
CREDIT ISSUES

WOODGATE & CO.

Chartered Accountant

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INSOLVENCY UPDATE

Terminating a winding up application

In *Deputy Commissioner of Taxation v Take A Seat Pty Ltd* the Federal Court of Australia was asked to terminate a winding up, three weeks after a Registrar of that Court ordered that the company be wound up.

The directors of the company advised that the company's failure to pay a statutory demand issued by the Australian Taxation Office ("ATO") was due to poor organisation and that the company was genuinely solvent. The directors advised the Court that their involvement with another business had reduced the company's liquidity but the other business had been closed and they were able to concentrate fully on the business of the company.

To the support the application the directors provided:

- an affidavit from the company's external accountant confirming that he would play a more active role in assisting them manage the financial affairs of the company;
- placed sufficient funds to pay all known creditors in their solicitor's trust account, supported by an irrevocable authority and

undertakings to the Court; and,

- undertook to ensure that all outstanding returns, required by the ATO, were lodged by the end of the following week.

Noting that neither the ATO or the Liquidator opposed the application, the Court ordered the termination of the winding up.

Administrators have themselves removed

Albarran v Young dealt with the application by two Administrators that their joint appointment be declared invalid.

The Receivers and Managers of several companies in a corporate group discovered that what appeared to be a wholly owned subsidiary company, which was not subject to their appointment. That company was the owner of a commercial office tower. A search of the ASIC database appeared to confirm the shareholding and the Receivers' and Managers' investigations suggested that the company was insolvent.

The Receivers and Managers took steps to bring the company within their control by convening an extraordinary general meeting of the company which

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passed resolutions purporting to replace the directors with two new directors. Those new directors then purported to conduct a meeting of directors, which resolved that the company was insolvent and that Administrators be appointed pursuant to Part 5.3A of the Corporations Act. The next day the Administrators became aware of concerns about the validity of that appointment and commenced an application to have their appointment declared valid.

The Administrators then discovered that there had been a change in ownership of the company and a consequent change in directors, prior to the purported extraordinary meeting. Concluding that the purported replacement of directors was ineffective, they formed the view that their purported appointment as Administrators was equally ineffective. They then amended their application to seek a declaration that their own appointment was invalid. Although satisfied that the Administrators were appointed in good faith, the Federal Court of Australia confirmed the Administrators' appointment was invalid.

Annulment of Bankruptcy

Baker v Rigg dealt with a bankrupt's application to the Federal Court of Australia to have her bankruptcy annulled. The circumstances of her debts were quite unusual. The debtor was the sole beneficiary of her husband's estate which had assets of almost \$1 million. The estate was liable to pay debts of \$130,000 arising from a business partnership with her nephew.

The debtor, her son and her nephew executed two deeds. The first deed, transferred all of the assets of the

debtor, including her share in the family home, to her son and her nephew. The second deed provided the debtor, her daughter and granddaughter, with the right to occupy the family home, rent free. The second deed also required the son and nephew to maintain the house and pay all taxes and charges.

The title was transferred and the debtor's nephew became sole owner of the house, which he mortgaged. Some time later the nephew defaulted in his payments to the bank. The bank began legal action to obtain possession of the property and sell it as mortgagee.

To stave off eviction, the debtor agreed to pay the interest that accrued on her nephew's debt. The debtor took legal action for negligence against the solicitor that had advised her about the two deeds and then took action against her nephew and her son based on claims of undue influence and unconscionable conduct. The debtor lodged a caveat on the family home and commenced legal action to uphold the caveat. However, after recognising that the caveat was defective she abandoned the application and agreed to pay the nephew's costs, who opposed the application.

The debtor was unsuccessful in Court. The nephew obtained judgment for the costs, her action against the solicitors was dismissed and the bank obtained judgment in relation to her promise to pay the interest. The bank then assigned that judgment to her nephew, on whose debt the interest was payable. The debtor then filed an appeal in relation to her claim of negligence against her solicitors.

The debtor vacated the family home

which was sold by the bank. The nephew served a bankruptcy notice on his aunt, filed a bankruptcy petition and then obtained a sequestration order by which she was made bankrupt.

The debtor wished to continue with her appeal in relation to the solicitor's negligence and the Trustee assigned the action to her daughter. The Court of Appeal of New South Wales upheld the daughter's right to continue the appeal but implied that it was likely to order security for costs. The daughter was unable to do so. That led to the debtor's application for annulment so that she could resume the action in her own name.

The Federal Court of Australia held that:

- it was not confined to the evidence before the Registrar who made the sequestration order and had discretion whether or not to annul a sequestration order;
- the nephew had breached his obligations under the deed and was liable to pay damages for that breach, even though no formal quantified claim had yet been made;
- at the date of the sequestration, the nephew was liable to pay damages to the debtor in an amount that would undoubtedly exceed the amounts which she owed to him at the date of sequestration;
- the appeal against the solicitors had substantial prospects of success because they took no steps to protect her against such a mortgage and did not warn her of the commercial risks to her; and,
- on those facts, a sequestration

order ought not to have been made and the bankruptcy should be annulled.

Adjournment of a winding up application

Deputy Commissioner of Taxation v Strongest Link Pty Limited concerned an Administrator's attempt to have a winding up application dismissed.

The evidence before the Court concerned a company that was involved in two large contracts. One contract was almost finished, with around 70 per cent of the work completed. Work on the second contract had not yet begun.

The Administrator estimated that if the company was to go into liquidation immediately, penalties would reduce the likely return from the first contract from \$318,000 to \$120,000. However, if the company expended approximately \$181,000 to complete the contract, it would provide a gross return of \$520,000. On that basis the creditors would be \$339,000 better off if the administration proceeded and the company completed the first contract.

The Administrator had proposed a Deed of Company Arrangement but there was no evidence before the Federal Court of Australia about whether the sole director and shareholder of the company would support that proposed Deed. The Administrator advised the Court he understood the director supported the proposal.

The Court was concerned that it was not clear whether the proposed Deed would make the whole of the net proceeds available for creditors but the Court held that that was ultimately a matter for negotiation between the

director and the creditors. The petitioning creditor being the ATO advised that a further small delay would not prejudice its position. Therefore, the Court allowed a further adjournment so that creditors were able to consider the proposed Deed.

made but stayed until after the date of the second creditors' meeting, so that a winding up order could be made promptly, if there was no agreement with creditors at the second meeting of creditors as to the proposal for a Deed of Company Arrangement

An order to dismiss the application was

WOODGATE & CO.

Chartered Accountant

Business Recovery Services

Registered Liquidator & Trustee in Bankruptcy

Level 14, 25 Bligh Street

Sydney, NSW, 2000

GPO Box 882, Sydney, NSW, 2001

Telephone: (02) 9233 6088 · Facsimile : (02) 9233 1616

www.woodgateco.com.au

Associated Offices in

Melbourne · Brisbane · Adelaide · Perth