CREDIT ISSUES

WOODGATE & CO.
Chartered Accountant
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INSOLVENCY UPDATE

Can assigned security secure pre-assignment debts?

In *Olympic Holdings Pty Ltd v Windslow Corporation Pty Ltd (In Liquidation)* the Supreme Court of Western Australia – Court of Appeal considered whether the assignment of fixed and floating charges could secure debts incurred, prior to the charges being assigned.

A company paid a $304,220 debt owed by a related company to its bank and took an assignment of the bank's two charges.

When the related company was placed into liquidation, the company claimed that the charges had all monies clauses, which secured debts that existed before the assignment, as well as debts created after the assignment.

The Court held that:

- there was no predisposition that a charge, if assigned, could not secure pre-assignment debts owed to the assignee;
- the ambit of an all monies clause should be determined according to ordinary principles of contractual construction. This included reference to the language of the contract, as well as a consideration of the purpose and object which the charge was apparently intended to achieve;
- in this case a proper construction of the charge documents led to the conclusion that pre-existing debts owed before the date of assignment were not secured monies, as defined in the documents; and,
- the debts allegedly incurred and owing after the assignment of the securities may be secured monies, as defined in the charges.

Guarantee or indemnity

A Trustee in Bankruptcy negotiated the settlement of a potential voidable transaction pursuant to Section 121 of the *Bankruptcy Act*, which was documented in a Deed apparently executed by a company and one of its three directors.

The company did not comply with the Deed and the Trustees commenced legal proceedings to ensure the company and the director complied with the Deed. Pursuant to the Deed, the company was required to pay the Trustees the sum of $500,000. The

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company was also required to pay within 12 months, the difference between $500,000 and half the value of the land, as determined by a valuation.

The company argued that the director did not have authority to bind the company and so the Deed was unenforceable. The director argued that if the Deed was unenforceable against the company, then it was also unenforceable against him, because his guarantee was discharged. The director also claimed that the Deed was ineffective because it had not been independently witnessed and that in any event execution had been procured by misrepresentation by the Trustees.

In *McIntosh v Linke Nominees Pty Ltd* the Supreme Court of Queensland held that:

- the source of the director's authority to act as agent for the company was not noted in the Deed. It was true that he held a majority of shares in the company. However, there was no evidence the other directors of the company were aware that he intended to compromise the Trustees' claim against the company;

- there being no representational conduct by the company or by any other director, the Deed did not bind the company and so the claim against the company must fail;

- execution of a Deed, witnessed by a solicitor for a party should not be held invalid, solely on that account;

- the director undertook to hold the Trustees harmless from any failure of the company to perform and was a co-beneficiary of the release provided by the Trustee;

- the director was an indemnifier as well as a guarantor and his obligation as an indemnifier survived a determination that the company was not bound by the Deed. The director would also be liable for damages for breach of warranty of authority; and,

- even if the representations claimed were in fact made, the Court was not satisfied that the director had relied upon them in executing the Deed.

The Court held that the director remained bound by the Deed and ordered he comply with the Deed.

Liquidator's remuneration

In *Conlan v Adams* the Supreme Court of Western Australia – Court of Appeal considered a Liquidator's claim for remuneration.

The Liquidator had convened a meeting of creditors pursuant to Section 473(3) of the *Corporations Act*, which declined to approve his remuneration. He then asked the Court to approve his claim.

At trial a Master of the Supreme Court of Western Australia adopted what it described as a broad-brush approach. The Master disallowed almost two-thirds of the remuneration claimed because the Liquidator had, at times, failed to conduct litigation in a cost-effective way, should not have been remunerated for other work pursuant to an indemnity provided by the Government of Western Australia and had not ensured that all work was conducted in a way that was of benefit to the creditors.

On Appeal the Liquidator argued that the Court could not utilise a broad-brush approach but should instead make specific adjustments based on specific issues. The Liquidator argued that the Master had taken into account an irrelevant consideration, namely the creditors' refusal to approve remuneration and stated that he had not sought payment for work pursuant to the indemnity with the State of Western Australia.

The Court held that:

- the Liquidator was not entitled to remuneration for work involving negotiating the indemnity or arranging payment pursuant to the indemnity;
- the evidence showed that the Liquidator's claim did not include work previously remunerated under the indemnity arrangement;
- although some of the work performed did not add value to the financial benefit of creditors, it was necessary in a general sense and reasonable;
- the Master had erred in adopting a broad-brush approach which did not consider specifics; and,
- the creditors' refusal to approve the remuneration claim was not an irrelevant consideration. However, the rejection of itself was of little weight in the absence of evidence as to creditors' reasons.

The Liquidator was mostly successful.

From 31 December 2007 the information required to be provided by Voluntary Administrators, Deed Administrators and Liquidators to Committees of Creditors, Committees of Inspection and meetings of creditors has significantly changed, pursuant to the *Corporations Amendment (Insolvency) Act* 2007. In particular, prior to convening a meeting to approve remuneration, a report must be prepared setting out:

(a) such matters as would enable an informed assessment as to whether the proposed remuneration is reasonable;

(b) a summary description of the major tasks performed or to be performed; and,

(c) the costs associated with each of those major tasks.

The Insolvency Practitioners' Association of Australia's Code of Professional Practice provides a useful benchmark to assess whether an insolvency practitioner's fees are necessary and proper.

Insolvent trading

After a four day hearing the Supreme Court of Queensland – Court of Appeal ordered two directors to pay $3,422,900 to the Liquidator of a company in respect of insolvent trading pursuant to Section 588G of the *Corporations Act*.

The directors appealed, identifying six grounds of Appeal. One of which was the alleged apprehended bias of the trial judge. At the hearing the directors abandoned those grounds and sought to raise new grounds.

The directors argued that they were not directors of the company at any relevant time, although the records of the Australian Securities and Investments Commission recorded them as directors. They also claimed to have been disadvantaged by the inability to have the alleged mental

incapacity of one director reviewed. Finally, they claimed that the Court had wrongly relied upon evidence of a former employee who had been charged with offences under the *Criminal Code (QLD)*.

In *Williams as Liquidator of Scholz Motor Group Pty Ltd (In liquidation) v Scholz* the Court held that:

- it would be unjust and inconsistent with judicial authority to allow the new grounds for Appeal to be raised. With one exception the issues raised on Appeal concerned issues which should have been raised at the original trial and it was difficult to see how any of the points could have succeeded on the evidence before the Court;

- evidence about the incapacity of a director would not have assisted his defence. Although incapacity might justify a director's inability to take part in the management of the company, it was clear that the director had in fact taken part in the management;

- the two directors had clearly acted as directors of the company pursuant to Section 9 of the *Corporations Act*, which was sufficient to bring them within the scope of the insolvent trading regime, regardless of any alleged deficiencies in the formalities of their appointment; and,

- a Court would arrive at the same conclusions, even if the evidence of the former employee was disregarded.

The Court dismissed the Appeal and awarded indemnity costs against the directors.

The case shows that Appeal Courts are reluctant to hear fresh evidence, which should have been presented at trial.

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