
CREDIT ISSUES

WOODGATE & CO.

Chartered Accountant

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INSOLVENCY UPDATE

Appointment of Provisional Liquidators

In *Beautree Pty Limited v Willow Glade Pty Limited* the Federal Court of Australia ("Federal Court") was asked to consider the appointment of Provisional Liquidators to two companies.

Willow Glade Pty Limited and Pazoluca Pty Ltd had two directors. One of the directors ("the first director") had become embroiled in Supreme Court litigation commenced by his former employer. The former employer alleged that the first director had misappropriated \$16M through the companies' creation of false invoices for goods or services not actually supplied.

That litigation had led to so-called freezing Orders being made against the two companies.

The two directors were unable to agree to a plan to deal with their companies' involvement in the litigation and the first director would not take telephone calls or respond to messages from the second director.

The second director asked the Federal Court to appoint Provisional

Liquidators to resolve the management deadlock. The former employer was granted leave to be heard and supported the Application, as potentially facilitating compliance with the Orders made by the Supreme Court of New South Wales.

The Federal Court held that:

- it was likely that winding up Orders would be made on just and equitable grounds at the final hearing because there was an irretrievable breakdown in the relationship between the two directors;
- whilst the freezing Orders made by the Court prevented the dissipation of assets, there was an urgent need for a change in control of the two companies to allow an appropriate and timely response in the Supreme Court proceedings; and,
- the need to address the possible insolvency of the companies was a further reason to appoint Provisional Liquidators.

The second director's Application for the appointment of Provisional Liquidators was successful.

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Liquidators' liability for post-appointment rent

Following the collapse of the high-profile Timbercorp group, the Liquidators of Timbercorp Securities Limited had to deal with a practical issue concerning rent owing for plantation land leased from numerous third parties and then sub-let to investors in managed investment schemes, which the company had promoted.

In their role as Administrators, the Liquidators had written to the Defendant, a landlord, seeking a standstill agreement by which the company would continue to use and occupy the land. However, the Administrators would not personally adopt any leases or be personally liable for rent. The letter explained that the standstill was proposed to give the Administrators time to finalise their investigations into the options available to the company.

The Defendant landlord did not agree to the proposed standstill agreement. The landlord's solicitors advised that the landlord would issue a Notice of Termination under the leases, if the rent was not paid when it was due. The solicitors stated that the 30 day contractual notice period would allow the Administrators' time to negotiate with the landlord.

The day before the rent was due, the Administrators became Liquidators pursuant to Section 446A of the *Corporations Act*. They wrote to the landlord confirming that, in their new role, they would likewise not adopt or ratify the leases.

The Liquidators did not want to

formally disclaim the leases. Although disclaiming the leases would completely release them from any liability for rent, it could adversely affect the investors who sub-let the land.

In *Timbercorp Securities Limited (in liquidation) v Plantation Land Limited* the Liquidators asked the Federal Court of Australia to clarify whether the post-appointment unpaid rent should be treated as an expense incurred by the Liquidators in carrying on business, which would have the effect of making it a priority claim pursuant to Section 556(1)(a) of the *Corporations Act*.

The Court held that:

- if a Liquidator elected to retain possession of leased land, a landlord was entitled to take action to recover rent;
- whether a Liquidator had elected to retain possession was determined objectively by reference to what the Liquidator had said and done;
- in this case the Liquidators were still considering whether or not to retain possession and they had not made a decision; and,
- the landlord could force the Liquidators to hurry up by serving a notice, under Section 568(8) of the *Corporations Act* requiring them to elect whether or not to disclaim the leases, but the landlord had not done so.

The Court ruled that the post-appointment rent was not a priority claim in the winding up because, on the facts, the Liquidators had not chosen or elected to retain possession of the leased land.

High Court rules

In *Vale v Sutherland* the High Court of Australia (“High Court”) considered the validity of a notice issued under Section 139ZQ of the *Bankruptcy Act*.

Section 139ZQ notices are issued by the Official Receiver to assist Bankruptcy Trustees recover voidable transactions. Non-compliance may result in imprisonment.

In this case the notice had been issued to the spouse of a bankrupt to recover the sum of \$270,000. That amount was calculated as the claimed value of the bankrupt’s half-share in land, based on a market assessment in 1998, which land had then been transferred to the spouse in 1999 for \$2. The commencement date of the bankruptcy was 20 February 2001. Therefore, the transfer was an under valued transaction pursuant to Section 120(1) of the *Bankruptcy Act*.

The spouse obtained an Order in the Federal Magistrates Court of Australia to set aside the notice on the grounds that it contained significant errors, including an incorrect description of a 1998 market appraisal by a real estate agent as a valuation and a calculation based on that appraisal value of \$540,000, rather than a valuation of \$417,000 conducted in 1999 by a registered valuer.

The Trustee appealed to the Full Court of the Federal Court of Australia, which

set aside the Federal Magistrates Court’s decision because, it ruled, those errors had not been raised in the spouse’s Defence or Cross-Claim. The spouse appealed to the High Court, arguing that the errors had been put in issue. In response the Trustee sought leave for a Cross-Appeal, claiming that the notice itself was conclusive and the spouse was not entitled to a review of the accuracy of the valuation recorded on the notice.

The High Court determined that:

- the spouse had raised his intention to challenge the \$540,000 value, so it was open to the Federal Magistrates Court to decide the case as it did;
- the 1999 valuation was undertaken by a registered valuer, less than a month before the transfer date and should be preferred to the 1998 appraisal, which was specifically disclaimed as an opinion of a reasonable asking price only and not to be taken as a sworn valuation;
- the Trustee’s leave to Cross-Appeal for payment of \$208,350 indicated belated acceptance that the 1999 valuation was better evidence of value than the appraisal; and,
- the Trustee was entitled to judgment for \$208,350 but on reasoning which differed from that upon which he succeeded in the Full Court. Therefore, the Trustee should pay the costs of the High Court Appeal.

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