
CREDIT ISSUES

WOODGATE & CO.

Chartered Accountants

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BEWARE OF LAST MINUTE TRANSACTIONS

Introduction

In the recent judgment of *Asden Developments Pty Ltd (in Liquidation) v Dinoris (No. 3)* [2016] FCA 788 a former Liquidator of the company was found to have contravened his statutory duties pursuant to Section 180(1) of the *Corporations Act 2001* (Cth) (*the Act*). That section provides that a director or officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would, if they were an officer of the company and occupied the same office and had the same responsibilities, having regard to the company's circumstances.

The main issue before the Federal Court of Australia was the failure of the former Liquidators to properly investigate the withdrawal of \$236,500 by Mrs Melinda Nichols ("Melinda"), the sole director of Asden Developments Pty Ltd ("Asden"), the day before Asden was wound up. The Court also considered whether, if a contravention occurred, Asden had suffered damage as a result.

The judgment was the latest in a series of cases involving the Nichols family.

Background

Asden was incorporated in 2005 for the

purpose of undertaking a land subdivision and residential development in Wakerley, Brisbane. The development was to be funded by the Nichols family, including Mr George Nichols ("George"). George's son, Mr Phillip Nichols ("Phillip"), was also involved in the development. However, as an undischarged bankrupt, he was legally unable to take part in the management of Asden. There was some evidence that Phillip was involved in the management of Asden as a de-facto director. Phillip's wife, Melinda, was also sole shareholder of Asden. Melinda did not contribute any funds towards Asden or the Wakerley development.

In 2006 land was purchased at Wakerley by the Nichols family. Subsequently the land ownership was divided into three, pursuant to a partnership between Mr and Mrs George Nichols, Mr and Mrs Peter Nichols, and Melinda. The land was subdivided into 10 lots, so that 10 properties could be developed, with five of the properties given to members of the Nichols family. The remaining five properties were to be sold for profit. George had been involved in previous property developments.

It was intended that Phillip and Melinda would gain property development

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experience by managing the development through Asden.

There were significant delays in the construction of the houses in the subdivision, possibly due to Phillip and Melinda's inexperience in managing construction contracts. By the end of 2010 the builder advised Asden and the Nichols family that a significant increase in funding was required to complete the development.

In October 2010 Melinda and Phillip separated. In November 2010 Melinda approached George and advised that Asden required more funding to pay its creditors. She also advised that she no longer wished to be involved in the management of Asden.

Between 4 December 2010 and 15 December 2010 George provided two cheques totalling \$270,000 to Asden to pay its trade creditors for debts incurred in the Wakerley development. It was alleged that the funds were held on trust to pay those creditors. The cheques were banked into Asden's account at Suncorp Bank. On 20 December 2010 the solicitor for the Nichols family demanded those funds be repaid.

Concerned about Asden's solvency, Melinda retained the services of Mr Peter Levis, a pre-insolvency adviser. On Mr Levis' advice, Melinda took the following steps:

- on 14 December 2010 Melinda incorporated TJI Investments Pty Ltd ("TJI"), of which she was the sole director and shareholder. A bank account was then opened for TJI with the Bank of Queensland ("BOQ");
- Melinda established a new bank account in Asden's name at the BOQ;
- on 15 December 2010, Melinda transferred the sum of \$264,500 from

Asden's Suncorp bank account to Asden's BOQ account;

- on 21 December 2010 Melinda withdrew \$236,500 from Asden's BOQ bank account and deposited it to Urban Property Group, an entity associated with Mr Levis. Following receipt of the funds from Asden, Urban Property Group deposited \$180,000 of those funds into the TJI BOQ bank account; and,
- on 22 December 2010, Asden was placed into creditors' voluntary liquidation and Messrs Dinoris and Combis, of Vincents Chartered Accountants, were appointed as joint and several Liquidators. The appointment was made by Asden, following a referral made by Mr Levis. According to the Liquidators, it was made clear that all queries regarding Asden were to be made to Mr Levis and not to Melinda.

On 22 December 2010 the Liquidators' office was informed by BOQ of the withdrawal of the \$236,500 by Melinda. On 23 December 2010 the Liquidators' contacted Mr Levis and asked him where the funds had been transferred. Mr Levis advised that the funds did not go to Melinda personally but encouraged the Liquidators to further investigate the withdrawal.

Breach of statutory duties

The Liquidators' made no direct enquiries with Melinda regarding the funds withdrawn from Asden's account. Mr Dinoris gave evidence that once he had conducted investigations of Asden's records of the withdrawal, he was concerned that attempts to contact the director would lead to the funds being dispersed. Melinda did not attend the meeting of creditors of Asden held on 7 January 2011 pursuant to Section 497 of *the Act*.

Mr Dinoris determined that the best approach was to conduct a public examination of Melinda and he unsuccessfully sought funding from creditors, particularly the Nichols family.

On 13 August 2013 consent Orders were made following separate proceedings which were contested. By Order of the Supreme Court of Queensland Messrs Dinoris and Combis were replaced as Liquidators of Asden by Mr David Clout of David Clout & Associates. The applicants were George and two other members of the Nichols family. The application was filed after evidence was given in related and wide ranging Family Court proceedings involving Melinda and the Nichols family.

The Federal Court found that although it was reasonable for Mr Dinoris to investigate Asden's records and seek funding from creditors to conduct a public examination of Melinda and others, this was not a sufficient substitute for a timely personal enquiry about her involvement in the transfer of funds. Mr Dinoris was found to have contravened his statutory duties pursuant to Section 180(1) of *the Act*. Despite being a joint and several Liquidator of Asden, Mr Combis does not appear to have been actively involved in the liquidation of Asden and the Court did not make any adverse findings against him.

Mr Dinoris was found by the Court to be unable to rely on the business judgment rule because Asden's complaint against him concerned the performance of his statutory duty as a Liquidator. It did not concern decisions made in the conduct of the business or commercial activity of Asden.

Did the Liquidator's breach of Section 180 cause damage to Asden?

The Court found that there was insufficient evidence to demonstrate that

Mr Dinoris' actions had led to damage to Asden. Justice Reeves examined the actions taken by Melinda in the days surrounding the transfer of the funds. He found that it was more than likely that, if the Liquidators had contacted Melinda and requested her to return the funds to Asden, she would have sought advice from either Mr Levis or her family law solicitor. Further, the Court found that there was sufficient evidence to suggest that either adviser, for different reasons, would have advised her not to repay the funds to Asden.

Therefore, the Court found that Asden had not established that it suffered damage from Mr Dinoris' contravention of Section 180. Subsequently, Asden was Ordered to pay Messrs Dinoris and Combis costs for the six day trial.

Conclusions

After Asden's winding up, the Wakerley development was completed by the Nichols family.

Following the completion of the development, George commenced proceedings against the builder to recover \$250,000 paid to the Master Builders Association as a surety for the development. Those funds were awarded to the builder by the Queensland Civil and Administrative Tribunal. Further, in 2012 George applied for statutory trustees for sale to be appointed to the five family properties. However, that process was delayed due to proceedings commenced by a creditor of Asden who had lodged a caveat on the properties in respect of a director's guarantee provided by Melinda. That creditor was eventually paid from the proceeds of sale of the properties.

The Wakerley development was a costly exercise for the Nichols family. A Family Court property proceeding between

Melinda and the Nichols family in 2013 determined a constructive trust existed for the \$270,000 advanced to Asden by George and withdrawn by Melinda. Judgment was awarded against Melinda, Mr Levis and her family law solicitor regarding the disbursement of those funds, plus costs. The legal costs incurred by the Nichols family in those proceedings were approximately \$171,000.

In May 2013 and July 2013 Melinda and Mr Levis, respectively, were declared bankrupt. The Nichols family lodged a Proof of Debt totalling \$9.65M in the liquidation of Asden.

There may have been reasons as to the structure employed in the Wakerley development. However, the combination of:

- a marriage breakdown;
- personal insolvency issues; and,
- a poorly timed and executed asset protection strategy,

resulted in significant costs and distraction from the resolution of commercial issues. This is all too often

evident in insolvency matters.

When a company enters into external administration it can be a distressing situation for the directors and officers of the company.

Directors frequently experience marital issues or personal insolvency at the same time, and often hope the problems associated with an insolvent company will simply disappear. As tempting as it may be to consult with an underqualified pre-insolvency adviser and arrange for them to take control of the insolvency process, it is important that directors are aware of their duties before and after the appointment of an external administrator.

This case demonstrates that Liquidators have a duty to adequately investigate transactions that come to their attention. Last minute transactions are fraught with danger. Liquidators who fail to properly investigate such transactions are at risk of removal, if an application is made to the Court pursuant to Section 503 of *the Act*.

We understand that Mr Clout is contemplating an Appeal.

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