CREDIT ISSUES

WOODGATE & CO.

Insolvency & Turnaround

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QUALIFIED PRIVILEGE IN INSOLVENCIES

Introduction

Qualified privilege operates as a defence to defamation in common law. It evolved in the 1760s in England in cases involving references given by masters about their servants. Qualified privilege was developed, because historically it was assumed that a defamatory statement was made maliciously. Therefore, the function of qualified privilege is to reverse the burden of proof of malice, so that it is borne by the Plaintiff.

When does it apply?

Qualified privilege operates in a number of circumstances, including:

(i) references for job applicants;
(ii) responding to police enquiries;
(iii) between teachers and parents;
(iv) between traders and credit reporting agencies;
(v) in building or tenancy matters involving a common landlord or neighbour(s);
(vi) between employers and employees; and,
(vii) where a legal duty exists which requires the disclosure of information, such as when an external administrator has been appointed to an insolvent company.

In insolvency

Section 89 of the *Corporations Act 2001* (Cth) ("the Act") codifies qualified privilege and provides protection from defamation, in the absence of malice. Qualified privilege is available under the Act to external administrators, auditors and certain persons providing information to the Australian Securities and Investments Commission ("ASIC").

External administrators are required to investigate the affairs of the company and, in certain circumstances, report to ASIC when appointed as:

(a) Receiver or Managing Controller pursuant to Section 422 of the Act;
(b) Voluntary Administrator or Deed Administrator pursuant to Section 438D of the Act; or,
(c) Liquidator pursuant to Section 533 of the Act. This excludes members' voluntary liquidations of solvent companies.

Whilst the wording of the three sections of the Act is not identical, external administrators must lodge reports with ASIC, when they suspect that offences have occurred under the Act, Australian law or where there are instances of negligence or misconduct in relation to a company. Additionally, a Liquidator must lodge a report with ASIC if unsecured creditors are likely to receive a dividend of less than 50 cents in the

dollar.

Qualified privilege is also available to Trustees in Bankruptcy, pursuant to Section 306B of the *Bankruptcy Act 1966* (Cth).

ASIC statistics disclosed that 99.8% of external administrators now lodge their reports electronically using the Schedule B questionnaire format, whether under Sections 422, 438D or 533 of the Act. The latest statistics from ASIC for the year ended 30 June 2016 recorded that 10,078 reports were lodged by external administrators. According to ASIC, external administrators reported possible misconduct in 82% of reports. The top three types of alleged misconduct reported by external administrators were:

(i) insolvent trading in 61% of reports;
(ii) failure to keep financial records in 42% of reports; and,
(iii) contraventions of directors' duties of care and diligence in 38% of reports.

Therefore, many of those reports could be considered defamatory.

Pursuant to Section 1274 of the Act, reports lodged under Section 422, 438D or 533 of the Act are not public records, which provides some protection to external administrators. Further, pursuant to Section 127 of the *Australian Securities and Investments Commission Act 2001* (Cth), ASIC is obliged to protect and assume confidentiality on information provided to it. Generally reports lodged under Sections 422, 438D or 533 of the Act will not be produced pursuant to applications to ASIC under the *Freedom of Information Act 1982* (Cth). However, such reports may be discovered in legal proceedings, as noted in *Lord v Commissioner of the Australian Federal Police* [1997] FCA 243.

Unintended consequences?

As a consequence of the *Insolvency Law Reform Act 2016* (Cth) ("ILRA") becoming effective on 1 September 2017, external administrators have new reporting obligations to creditors. Reports such as Voluntary Administrators' reports and Liquidators' three monthly dividend reports, are now required to be lodged at ASIC. Hence they are public documents. Whilst Sections 442E and 535 of the Act provide some protection to Administrators and Liquidators for statements made orally or in writing, it may be that because of the ILRA, external administrators find themselves defending spurious and costly defamation claims from disgruntled company directors and/or creditors. Surely this would be an unintended consequence of the ILRA.

Conclusion

Perhaps the best protection from such claims is to ensure that all correspondence and public documents are prepared with care, as noted in *Samsun Pty Ltd v Andrew Wily* [2000] NSWSC 281, in which a Liquidator successfully defended a defamation claim arising from a press release.

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