



BUSINESS ADVISORS & INSOLVENCY SPECIALISTS

Insolvency Communique

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Liquidator suspended

Dean-Willcocks v Companies Auditors and Liquidators Disciplinary Board concerned a liquidator's appeal against a decision to suspend his registration as a liquidator.

The Companies Auditors and Liquidators Disciplinary Board ('CALDB') held that the liquidator had accepted appointments when he had a conflict of interest, and had failed to tell creditors that he had a possible conflict of interest in accepting other appointments.

The conflict of interest was said to arise by reason of a joint-venture agreement in which the liquidator's firm and an accounting practice agreed to cross-refer clients.

The liquidator argued that he had complied with all of the requirements of the *Corporations Act*, and that the ethical rules of professional associations were not relevant. The liquidator advised that the non-disclosure was in accordance with legal advice he had received, and argued that a conflict of interest arose only if there was a 'real' or actual conflict.

The Court held that:

- The duties specified in the *Corporations Act* were not expressed to be exclusive.
- The question of whether a person properly carried out their duty is not a pure question of law and required consideration of accepted professional standards.
- It was possible to conclude that a person had failed to properly carry out their duty without identifying the breach of a statutory provision.
- It was not necessary for the CALDB to assess the detailed circumstances of any particular appointment to identify situations that created a real possibility of impairing independence.

- It was open to the specialist CALDB to give such weight to the professional standards as it saw fit, and on the evidence, it was open to arrive at the conclusions that it did.

The Court declined to reverse the CALDB finding and - notwithstanding 'outstanding' character references and 'very laudatory remarks by...leading figures in the insolvency industry' - also declined to reduce the twelve month suspension.

Enforcement of charge to associated person

In Highland v Exception Holdings Pty Ltd (in Liquidation) & Anor the New South Wales Supreme Court was asked to consider the operation of section 267 of the *Corporations Act*.

Section 267 operates to void a charge granted in favour of a director or director's associate if it is enforced within six months of its creation without the prior approval of the Court.

In this case the charge was granted to two directors, but in their capacity as executors of the estate of a third director and shareholder of the company, prior to their replacement by the director's widow as administrator of the estate.

The widow argued that because the charge was granted to them as trustees, not in their personal capacity, they received no benefit and section 267 should not apply.

The Court of Appeal held that:

- The charge had been executed in a 'very peculiar way' under a power of attorney which pointed to the two directors 'acting in concert in their respective capacities.'
- Section 267 did not proscribe creation of a charge in favour of an associated person or render it void - it was only enforcement that could trigger avoidance.

- The ‘mischief’ that section 267 was intended to address was a director’s early exercise of enforcement powers to take unfair advantage over other creditors - and this could arise even if the charge was taken in a representative capacity.
- If section 267 did not apply to directors in a representative capacity then it could be easily defeated by taking a charge for the benefit of a discretionary trust.

The charge was held to be void.

Insolvent trading

Ho v Akai Pty Limited (In Liquidation) dealt with a liquidator’s claim for insolvent trading.

The company now in liquidation had been negotiating with a ‘white knight’ - a potential purchaser of the business - and had signed a ‘management authority’ which authorised the white knight to manage its business.

However, the white knight did not proceed with the rescue, and the company passed into administration and later liquidation.

The liquidator commenced an insolvent trading claim against the white knight and some of its senior managers, arguing that they had acted as directors of the company and should be made liable for the debts incurred when it was insolvent and under their management.

As a preliminary point, the alleged shadow directors argued that the liquidator had not established a prima facie case against them. The senior managers argued that they had acted under the instructions of their employer and that any claim should be directed against their employer only.

The Full Federal Court of Appeal held that:

- Prima facie the directors of the failed company regarded themselves as bound to follow the instructions of the white knight, and those whom they regarded as speaking on its behalf.
- Although it appeared that at least some of the senior managers may not have been involved in the day-to-day management of the failed company, they appeared to be involved at a strategic level, and it was at least arguable that they had acted as shadow directors.
- The authority provided by the Management Agreement was ‘widely cast’ covering ‘without limitation all financial, operational, legal, corporate, administrative and other matters.’ However, it did not operate to make the company a subsidiary of the white knight, and for that reason the liquidator’s alternate ‘holding company’ claim was not sustainable.

The attempt to prevent the liquidator proceeding to full trial was unsuccessful.

Loan account or remuneration?

In *Pascoe & Anor v. Duarte* the New South Wales Supreme Court was asked to consider whether amounts totalling \$1.35 million was remuneration paid to a director – but recorded incorrectly as a loan in the company’s books – or whether it was truly a loan and therefore recoverable by the liquidator

Each side had evidentiary difficulties. The liquidator was unable to refer to a formal document evidencing a loan, however the director was unable provide any contemporaneous records evidencing regular payments of monies as salary or wages to the defendant.

The director explained that he was the sole controlling executive of a large recruitment business with between 400 to 500 employees generating revenue of many millions of dollars. He argued that he was entitled to be remunerated on the scale he claimed, and said that the accounts referred to by the liquidator were draft accounts that had never been adopted.

The Supreme Court held that:

- As neither party contended that the payments were made by way of gift, the question before the Court was whether the monies were loan monies or remuneration.
- The amounts paid to the CEO were significantly in excess of the income disclosed in his tax return.
- There was no evidence of any agreement in the company to make payments to the CEO as wages or salary.
- At no time did the CEO or anyone acting on his behalf specifically treat the monies paid to him as any form of remuneration.

For that reason the evidence strongly pointed to a loan account as claimed by the liquidator.

There was a minor adjustment to the amount claimed, however the liquidator was successful in obtaining an order for the recovery of \$1.16 million.

Important note

The information contained in this newsletter is by way of general comment only and is not intended as a substitute for specific advice that addresses your particular circumstances. You should seek specific advice before acting.

PATTISON v COOK**[2006] FMCA 1713**

During the course of the administration of the bankrupt estate, the bankrupt informed the trustee on various occasions that she intended to bring proceedings against the trustee in relation to his administration of the estate.

The bankrupt did not specify the nature of the claim upon which such legal proceedings would be based.

There were sufficient funds in the estate to pay the bankrupt's debts, but the trustee was not willing to issue a certificate of annulment under Section 153A of the Bankruptcy Act, 1966 in light of the litigation threatened by the bankrupt, which would have meant that the administration could not be finalised with certainty.

Accordingly, the trustee brought an application seeking orders that the bankrupt issue any proceedings against him in relation to the administration of the estate within 3 weeks, failing which the bankrupt's debts be paid and the bankrupt be stayed from issuing any proceedings against the trustee in relation to the administration of the bankrupt estate. The Court granted the application. This case follows the authority of *Bellin v Pattison* [1999] FCA 51.

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