Ground Floor

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Voidable transactions under the Corporations Act: something old and something new

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Introduction

1. There are parts of the *Corporations Act* which, at least in terms of heritage are very old, and parts which are very new. In this paper, I consider one from each category.

The Old: Section 588FE(5) of the *Corporations Act*

2. Whilst the wording of section 588FE(5) dates only to the corporate law reforms of 1993, the heritage of the provision is far older. Together with section 121 of the *Bankruptcy Act,* section 37A of the *Conveyancing Act* (NSW) (and like provisions in the other States[1]), section 588FE(5) traces its origins to the *Fraudulent Conveyances Act 1571* (13 Elizabeth 1, c 4 & 5) (the ***Elizabethan Statute***), one of the earliest attempts in English law to deal with voidable transactions.

3. The strident tones of the preamble to the Elizabethan Statute give a vivid insight in to the mischief which the drafters considered needed to be addressed. A readable translation of the old English drafting being:

> "For the avoiding of feigned, covinous and fraudulent feoffments, gifts, grants, alienations, bonds, suits, judgments and executions, as well of lands and in tenements, as of goods and chattels, more commonly used and practised in these days than hath been seen or heard of heretofore; which feoffments, gifts, grants etc have been and are devised and contrived of malice, fraud, covin, collusion or guile to the end, purpose and intent to delay, hinder or defraud creditors and others of their just and lawful actions, suits, debts, etc; not only to the let or hindrance of the due course and execution of law and justice, but also to the overthrow of all true and plain dealing, bargaining and chevisance between man and man, without the which no commonwealth or civil society can be maintained or continued.
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> Be it therefore declared, ordained and enacted, that all and every feoffment, gift, grant, alienation, bargain and conveyance of lands, tenements, hereditaments, goods and chattels, or any of them, by writing or otherwise, and all and every bond, suit, judgment and execution at any time had or made to or for any intent or purpose before declared and expressed, shall be from henceforth deemed and taken, only as against that person or persons, his or their heirs, successors, executors, administrators and signs of every of them, whose actions, suits, debts, etc; by such guileful, covinous or fraudulent devices and practices, as is aforesaid, are, shall or might be in anywise disturbed, hindered, delayed or defrauded, to be clearly and utterly void, frustrate, and of none effect, any pretence, colour feigned consideration, expressing of use or any other matter or thing to the contrary notwithstanding.
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> Provided that this act or anything therein contained shall not extend to any estate or interest in land, tenements, hereditaments, leases, rents, commons, profits, goods or chattels, had, made, conveyed or assured, or hereafter to be had, made, conveyed or assured, which estate or interest is or shall be, upon good consideration and bona fide, lawfully conveyed or assured to any person or persons, or bodies politic or corporate,

[1] Civil Law (Property Act) 2006 (ACT), s 239; *Law of Property Act 2000* (NT), s 208; *Property Law Act 1974* (Qld), s 228; *Law of Property Act 1936* (SA), s 86; *Conveyancing and Law of Property Act 1884* (Tas), s 40; *Property Law Act 1958* (Vic), s 172; *Property Law Act 1969* (WA), s 89.

not having at the time of such conveyance or assurance to them made any manner of notice or knowledge of such covin, fraud or collusion as is aforesaid."

4. The words of the statute give a very strong flavour of the assault which its drafters felt these types of conveyances represented to "society, law and justice", noting its statement that fraud was "more commonly used and practised in these days than hath been seen or heard of heretofore". This sentiment was echoed in 1601 in *Twyne's case*[2] where the Court of Star Chamber lamented that "fraud and deceit abound in these days more than in former times", and resolved that "all statutes made against fraud should be liberally and beneficially expounded to supress the fraud".[3]

5. The Statute of Elizabeth was apparently considered so effective in suppressing fraudulent conveyances that, other than minor amendments, the Act remained in force both in England and later in the colony and State of NSW for the next 340 years. In 1924,[4] the wording was streamlined and modernised and "substitution" of the new words made by the *Property (Amendment) Act 1924* (UK):

"(1) Save as hereinafter provided, every conveyance of property made whether before or after the commencement of this Act, with intent to defraud creditors, is voidable, at the instance of any person thereby prejudiced.

(2) This provision does not (a) affect the operation of a disentailing assurance, or the law of bankruptcy for the time being in force; or (b) extend to any estate or interest in property conveyed for valuable consideration and in good faith, or upon good consideration and in good faith, to any person not having, at the time of the conveyance, notice of the intent to defraud creditors."

6. The following year, 1925, the Elizabethan Statue was formally repealed and replaced by section 127 of the *Law of Property Act* (UK), which differed only in minor respects from the 1924 wording.

7. New South Wales followed suit from 1 January 1931, with the coming into force of amendments which repealed the Elizabethan Statute and added section 37A to the *Conveyancing Act* in the following terms:[5]

37A Voluntary alienation to defraud creditors voidable

(1) Save as provided in this section, every alienation of property, made whether before or after the commencement of the *Conveyancing (Amendment) Act 1930*, with intent to defraud creditors, shall be voidable at the instance of any person thereby prejudiced.

(2) This section does not affect the law of bankruptcy for the time being in force.

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[2] (1601) 76 ER 809

[3] May, Henry W. (Henry William) & Edwards, William Douglas, 1848- (1908). '*The law of fraudulent and voluntary conveyances: being a treatise on the statutes of Elizabeth against fraudulent alienations, and on the law of voluntary dispositions of property*' (3rd ed. / by W. Douglas Edwards). Stevens and Haynes, London

[4] *Law of Property (Amendment) Act 1924* (UK), Schedule 2, item 31; *Law of Property Act 1925* (UK), Part IX, s 172.

[5] *Conveyancing (Amendment) Act 1930* (NSW), ss 2, 10 and Schedule.

(3) This section does not extend to any estate or interest in property alienated to a purchaser in good faith not having, at the time of the alienation, notice of the intent to defraud creditors.

8. However, the revision of the language of the Elizabeth Statute made no changes to the purpose of the provision. In an echo of *Twyne's Case,* over four hundred years earlier, in *Hall v Poolman,*[6] Palmer J observed:

> "The purpose of s 37A is to defeat fraud no matter by what device it is implemented. The reach of the section is not foreshortened by technical obstructions placed in the way of recovery proceedings in furtherance of the original fraudulent intent. The words of the section are of the widest possible application; they focus on the effect of what is done, not on the means by which it is done."

9. Since proof of intention is notoriously hard to prove, over the course of centuries, Courts had come to accept that proof of fraudulent intention could be inferred from the circumstances in which the transfer was made, rather than it needed to be proven that the person making the payment had a subjective intention to defraud. The classic statement of this type of approach was the statement of Hatherley LC in *Freeman v Pope*[7] in 1870, where his Lordship said:

> [I]n the absence of…direct proof of intention, if a person owing debts makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid, then, since it is the necessary consequence of the settlement…that some creditors must remain unpaid, it would be the duty of the Judge to direct the jury that they must infer the intent of the settlor to have been to defeat or delay his creditors, and the case was within the [Elizabethan] statute.

10. As mentioned, the Elizabethan Statute was the progenitor of section 121 of the *Bankruptcy Act.* As currently formulated that section says:

Transfers to defeat creditors

Transfers that are void

(1) A transfer of property by a person who later becomes a bankrupt (the transferor) to another person (the transferee) is void against the trustee in the transferor's bankruptcy if:

(a) the property would probably have become part of the transferor's estate or would probably have been available to creditors if the property had not been transferred; and

(b) the transferor's main purpose in making the transfer was:

(i) to prevent the transferred property from becoming divisible among the transferor's creditors; or

[6] (2007) 215 FLR 243; [2008] NSWSC 1330 at [550].
[7]

(ii) to hinder or delay the process of making property available for division among the transferor's creditors.

11. Prior to the reforms introduced into the *Corporations Law* by the *Corporate Law Reform Act 1992,* section 565(1) of the *Corporations Law* (Cth) provided that a transfer of property by a company that, if it had been made by a natural person, would be void against a trustee in bankruptcy was likewise void against the liquidator. However, post the 1992 reforms,[8] the operation of section 565(1) was limited to transfers occurring before 23 June 1993 and the code now found in Part 5.7B of the Act dealing with voidable transactions was inserted. Since that time stated that, subject to the company being wound up and the transaction being after 23 June 1993, a transaction is a "voidable transaction" if:

(a) it is an insolvent transaction of the company; and

(b) the company became a party to the transaction for the purpose, or for purposes including the purpose, of defeating, delaying, or interfering with, the rights of any or all of its creditors on a winding up of the company; and

(c) the transaction was entered into, or an act done was for the purpose of giving effect to the transaction, during the 10 years ending on the relation-back day.

12. Section 588FE(5) is thus an amalgam of concepts arising from the 1992 reforms, with the much older concept of defeating creditors. It is also probably the least examined species of voidable transaction, and one which many practitioners are least familiar with.

The Elements of section 588FE(5)

13. To succeed in a claim under section 588FE(3) the Liquidator (for subject to what I will discuss later, these are claims must be brought by a liquidator), must prove four elements.

14. First there must be a "transaction" as defined in section 9 of the Act. That definition requires that the company itself be a party to the relevant transaction, although Courts have accepted that a "transaction" for the purposes of the definition can be a series of steps, so long as they are connected which give an outcome or result rather than being limited to, for example, a particular payment or transfer.[9]

15. Second, that transaction in question is to be an "insolvent transaction". Under section 588FC an unfair preference, or an uncommercial transaction are insolvent transactions if, at the time they were made, the company was insolvent or it became insolvent because of entering into the transaction.

16. The third element is the "purpose element", which largely adopts the language of the Elizabethan Statute, and goes to the issue of intention, which I will return to shortly.

[8] *Corporate Law Reform Act 1992,* s 104

[9] See *Capital Finance Australia Ltd v Tolcher* per Lindgren J.

17. Finally, the liquidator needs to show that the transaction in question was entered into or something done to give effect to it within 10 years before the relation-back day.

The Insolvent Transaction Element

18. Since a voidable transaction under section 558FE(5) must always be an "insolvent" transaction under section 588FC, the only reason a liquidator would resort to section 588FE(5) is where issues of time arise.

19. Under section 588FE(2), a transaction is voidable if it is an insolvent transaction (namely an unfair preference or an uncommercial transaction) and it was entered into or something done to give effect to it within six months before the relation-back day.

20. Under section 588FE(3), a transaction is voidable if it is an insolvent transaction (namely an unfair preference or an uncommercial transaction) and it is also an uncommercial transaction, and it was entered into or something down to give effect to it within 2 years.

21. It is here that section 588FE(5) potentially comes into play. What section 588FE(5) does is allows the liquidator the ability to reach further back in time beyond the 6 months for unfair preferences in section 588FE(2) and beyond the 2 years for uncommercial transactions in section 588FE(3) respectively: the *quid pro quo* being that to do so, the liquidator must make out the additional "purpose element".

The "Purpose Element"

22. Read in insolation, the "purpose element" sets a daunting bar, and despite early cases such as *Freeman v Pope,* from the 1930s in particular cases, the High Court began to take a stricter and more subjective approach to the proof of intention to defraud. The high point of this approach probably came in the 1998 case of *Cannane v J Cannane Pty Ltd (in liq)*[10](***Cannane***), where the majority of the High Court held that whilst a court could use the surrounding circumstances to infer that the relevant "purpose" of defrauding creditors was present, the use of inferences from the circumstances did not overcome the necessity to demonstrate some "element of dishonesty" at the time of the transaction in question and to prove a "real" and "actual" intention. Thus in *Cannane*, Gummow J said, in respect of the intention element at [27]:

> The expression "with intent to defraud" does not have any universal connotation applicable in all statutory contexts in which it is found. However, the appellants properly relied upon a passage in the judgment of Dixon CJ in *Hardie v Hanson*. This case arose under s 281 of the *Companies Act 1943* (WA) and concerned the personal responsibility of a director for the debts or other liabilities of a company whose business had been carried on in the course of the winding-up "with intent to defraud creditors of the company or creditors of any other person". Dixon J said:
>
> > "The phrase 'intent to defraud creditors of the company' suggests that present or future creditors of the company will, if the intent is effectuated, be cheated

[10] [1998] HCA 26; 192 CLR 557

> of their rights. An intent to defraud creditors has been described, for the purposes of bankruptcy legislation, as an intent by deceit to deprive creditors of something to which they are entitled".

In the same case, Kitto J said that the onus lay on the liquidator:

> "to prove affirmatively that the carrying on of the company's business during the relevant fifteen months was characterised by an intent - which in the circumstances means an intent on the part of [the director] - to defraud creditors of the company. An actual purpose, consciously pursued, of swindling creditors out of their money had to be established against [the director] before a declaration under the section could be made."

23. Gaudron J, in *Cannane*, said, at [31]:

> "It is to be remembered that the operation of s 121(1) depends on the intent of the bankrupt or, where it is applied in a company winding up, the intent of the company concerned. What is in issue in each case is, as Dixon J said in Williams v Lloyd; In re Williams, a "real intent". And as Starke J observed in the same case, "Frau ... is not to be presumed". That is not to deny that it may take very little to justify a finding of fraud or intent to defraud for the purposes of s 121(1) of the Act if the person or company concerned disposes of assets when facing financial difficulties. Even so, the real intent must be ascertained."

24. The effect of these comments was summed up in 2009, by Hong Kong Court of Final Appeal,[11] as follows:

> "The majority of their Honours therefore appear, obiter, to have relegated the depletion of a fund as a result of a voluntary disposition by an insolvent debtor with the probable or inevitable consequence of defeating or delaying creditors into "material from which an inference of intent to defraud…might be drawn" That is a considerable distance away from the line of cases which regarded such facts as giving rise either to an irrebuttable presumption or to an irresistible or near irresistible inference of an intent to defraud."

25. However, whilst this was approach in Australia, in 2009 the Supreme Court of New Zealand had cause to consider the correct approach to the proof of intention in *Regal Castings v Lightbody,* [2009] 2 NZLR 433. In that decision, the joint judgment of Blanchard and Wilson JJ with whom McGrath J agreed, said in relation to the inference of intention (at 457):

> "Whenever the circumstances are such that the debt must have known that in alienating property, and thereby hindering, delaying or defeating creditors' recourse to that property, he or she was exposing them to a significantly enhanced risk of not recovering the amounts owing to them, then the debtor **must be taken to have intended this consequence, even if it was not actually the debtor's wish to cause them loss**"

[11] *Tradepower (Holdings) Limited (in liq) v Tradepower (Hong Kong) Ltd & Ors* [2009] HKCU 1889 at [75],

26. The ongoing effect which the High Court's decision in *Cannane* on Australian jurisprudence up to 2011 in this area was demonstrated in *Marcolongo.* On appeal to the NSW Court of Appeal, on the basis of *Cannane* Allsop J, said that whilst in some cases inference but be used, the "central question" which the trial judge had not addressed as being whether the transferor "had actual and real intention" to defraud the creditor and Young JA indicated that there was a requirement of "some element of dishonesty".

27. However, on the subsequent appeal to the High Court, the plurality endorsed as correct the statement made by *Regal Castings* to the effect that it was unnecessary to show that the debtor wanted creditors to suffer a loss or that the debtor had a purpose of causing loss. Whilst it was necessary to show the existence of an intention to hinder, delay or defeat creditors and *in that sense* to show that accordingly the debtor had acted dishonestly.[12] This could be inferred. The High Court did not endorse any requirement to show an "actual intent" in sense of animus by an awareness that the transaction would have an effect on the ability of creditors to recover from the transferor.[13]

28. Their Honours also endorsed the remarks of Russell LJ in *Lloyds Bank v Marcan*. When his Lordship said:

> "I am not sure what is meant by a perfectly innocent defeat, hindrance or delay. It must be remembered that in every case under this section the debtor has done something which in law he has power and is entitled to do: otherwise it would never reach the section. **If he disposes of an asset which would be available to his creditors with the intention of prejudicing them by putting it, or its worth, beyond their reach, he is in the ordinary case acting in a fashion not honest in the context of the relationship of debtor and creditor.** And in cases of voluntary disposition that intention may be inferred ... The intention of Mr Marcan is perfectly plain: the lease to his wife was designed expressly to deprive the bank of the ability to obtain the vacant possession to which the bank plainly attributed value, and to diminish to that extent the strength of the bank's position as creditor. To take that action at that juncture, in my judgment, was, in the context of relationship of debtor and creditor, less than honest: it was sharp practice, and not the less so because he was advised that he had power to grant the lease. It was, in my judgment, a transaction made with intent to defraud the bank within s 172, and would have been within the [Elizabethan] Statute."
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> [Footnotes omitted and emphasis added]

29. Their Honours noted, a person may have acted dishonestly, judged by the standards of ordinary decent people, without appreciating that the act in question was dishonest by those standards.[14]

30. Finally, in respect of a submission that *Cannane* required "the onus of proving actual intent" the plurality distinguished that phrase, by explaining that in using the word

[12] at [32]
[13] ibid
[14] at [33], citing *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*

"actual" the judges in *Cannane* were merely meaning that "while the existence of the intent might be inferred from the evidence, it was to be found as a fact."[15]

31. The effect of *Marcolongo* was summarised by Sackar J in Joanne *Elizabeth Young v Josephine Aapa Smith*,[16] as follows:

> "[37] It is not necessary, for the purposes of s 37A, that there be actual proof that the alienator had in his mind an intention to defraud creditors; the court can attribute to the alienator the requisite fraudulent intent if, from all the surrounding circumstances, it appears that the effect might be expected to be, or has in fact been, to defeat creditors: Re Trautwein; Richardson v Trautwein (1944) 14 ABC 61 at 75 per Clyne J, cited with approval by the Full Court of the Federal Court of Australia in PT Garuda Indonesia Ltd v Grellman (1992) 35 FCR 515 at 523. **The relevant intention need not be a predominant or sole intention**; Marcolongo v Chen at [57] and [58]. As Heydon J pointed out in Marcolongo v Chen, the section does not postulate a mixture of motives from which there must be extracted a predominant intention to defraud: Marcolongo v Chen at [25]

His Honour then cited with approval the passage from *Freeman v Pope,* quoted above.

32. In *Commissioner of Taxation v Oswal and Anor* (No 6)[17] at [66] Gilmour J set out the "various circumstances in which it is recognised that the Court will move readily to infer the existence of the requisite intention", which, for the purposes of 588FE(5), relevantly include that:

1. The "natural and probable consequences" of the disposition is the defeat or delay of creditors;
2. The alienation is made voluntarily;
3. The alienation is made in favour of a family member; and
4. The alienation is made in haste or proximately to one or more events indicating financial stress on the part of the company.

33. In the words of the High Court, evidence of this species has sufficient weight to "entitle the fact finder to decide an issue (here the necessary intent) in favour of the moving party, although the fact finder is not obliged to do so and other evidence given may be decisive to the contrary".[18]

34. In the case of section 588FE(5), the purpose in question does not need to be the main purpose or the sole purpose. In *Ashala Model Agency Pty Ltd (in liq) & Anor v Featherstone & Anor* [2016] QSC 121, the only available decision on section 588FE(5) I have been able to locate, Jackson J said:

[15] at [34]
[16] [2015] NSWSC 400
[17] (2016) 339 ALR 560; [2016] FCA 762
[18] *Marcolongo* at [25]

> “[166] The words “or for purposes including the” have the effect that the identified purpose need be only one of the purposes that cause the company to enter into the transaction. Accordingly, if the second plaintiff can show that the first defendant’s intention and therefore the first plaintiff’s purposes were in part to defeat, delay or interfere with any or all of its creditors, that will be enough to engage s 588FE(5), if the other elements are satisfied.
>
> [167] This is not the same as the requirement of a “main” purpose under s 121(1) of the BA as discussed in The Trustee of the Property of Cummins v Cummins.[39] As a matter of ordinary meaning, a “main” purpose will usually be something greater in degree than any other purpose. There is no such requirement under s 588FE(5).”

35. Ultimately, each case will turn on its particular facts and the totality of the circumstances, however in the wake of the clarification of the position which *Marcolongo* has now provided with respect to the “purpose element”, liquidators may feel more comfortable invoking section 588FE(5) that has been the case so far. By analogy to section 37A, the reasoning in *Marcolongo* stands for the proposition that it is unnecessary for the liquidator to show that the company (or its guiding mind) wanted the creditors to suffer a loss or that it had the purpose of causing such loss, instead it is necessary to show that *a* purpose was to defeat, delay or hinder creditors and *in that sense* to show that the company has acted dishonestly.

Defences

36. Like all voidable transactions, the defence in section 588FG(1) applies to claims voidable transactions under section 588FE(5). That section says:

> “(1) A court is not to make under section 588FF an order materially prejudicing a right or interest of a person other than a party to the transaction if it is proved that:
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> (a) the person received no benefit because of the transaction; or
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> (b) in relation to each benefit that the person received because of the transaction:
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> (i) the person received the benefit in good faith; and
>
> (ii) at the time when the person received the benefit:
>
> (A) the person had no reasonable grounds for suspecting that the company was insolvent at that time or would become insolvent as mentioned in paragraph 588FC(b); and
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> (B) a reasonable person in the person's circumstances would have had no such grounds for so suspecting.”

Utility of section 588FE(5)

37. In circumstances where there is an otherwise good unfair preference claim or an uncommercial transaction claim which is time barred by operation of section 588FE(2) or 588FE(3) section 588FE(5) may provide an alternative route to recovery.

38. Whilst it is correct that the allegation that a purpose in making the transaction is a serious allegation and not to be made lightly, the decision in *Marcolongo* has clarified that proof of purpose is not as onerous as the decision in *Cannane* had been taken to suggest and judges post *Marcolongo* have indicated a readiness to accept that intention can be inferred from the circumstances. Last year, in *Ashala Model Agency Pty Ltd (in liq) & Anor v Featherstone & Anor* [2016] QSC 121, the only case I was have been able to located where a liquidator invoked section 588FE(5), the liquidator was successful.

39. In short, liquidator should not write off claims for unfair preferences or uncommercial transactions outside the time limits in section 588FE(2) and (3) without at least giving some consideration to whether those claims might fall within section 588FE(5). Whilst uncommonly used, recent developments may mean it has a greater role to play in corporate law going forward.

***The New*: Section 100-5 of the Insolvency Practice Schedule (Corporations)**

40. On 1 March 2017, a new Schedule 2 was added to the *Corporations Act* a new section 600K was added to the Act which provides that "Schedule 2 has effect".[19]

41. Within Schedule 2 is section 100-5 provides as follows:

> **100-5 External administrator may assign right to sue under this Act**
>
> (1) Subject to subsections (2) and (3), an external administrator of a company may assign any right to sue that is conferred on the external administrator by this Act.
>
> (2) If the external administrator's action has already begun, the external administrator cannot assign the right to sue unless the external administrator has the approval of the Court.
>
> (3) Before assigning any right under subsection (1), the external administrator must give written notice to the creditors of the proposed assignment.
>
> (4) If a right is assigned under this section, a reference in this Act to the external administrator in relation to the action is taken to be a reference to the person to whom the right has been assigned.

42. That section stems from a proposal paper published by the Australian Government in December 2011.[20] That paper relevantly said at [216] – [218]:

> "216. Reforms are proposed to allow practitioners to assign causes of action. This would increase the level of deterrence against corporate breaches, reduce

[19] Note however that this statement is apt to mislead given that certain elements within Schedule 2 do not become operative until 1 September 2017. See, generally, *Re Glengrant Civil Pty Ltd (in liq)* [2017] NSWSC 843.
[20] *Proposals paper: A modernisation and harmonisation of the regulatory framework applying to insolvency practitioners in Australia*

losses suffered by stakeholders as a result of those breaches and increase the overall efficiency in insolvency administrations.

216.1. There is some uncertainty as to whether statutory rights of action arising under the Corporations Act may be sold. The statutory powers of insolvency practitioners would be amended to clarify that a practitioner is empowered to assign statutory rights of action arising out of the Corporations Act that vest with the practitioner (or company) during an administration, to a third party.

217. The ability to take civil action to recover company property inappropriately dissipated prior to business failure and hold directors liable for insolvent trading are key mechanisms to address phoenix activity.

218. The inability to obtain funding is a major obstacle to the commencement of these actions. The taking of these actions may also delay the finalisation of administrations as a whole, ultimately to the detriment of creditors. The sale of rights of action may enable the value in such rights to be realised in the absence of funding being available and may result in the pursuit of matters which would not otherwise have been able to be pursued."

What types of claims does section 100-5 apply to?

43. The "rights to sue" conferred upon an "external administrator", relevantly a liquidator, by the Corporations Act fall into two classes.

44. First, sections 588M(2) and 588W(1) give a liquidator a right to "recover" as a debt due to the company, an amount equal to the amount of the loss or damage to the company. In other words, the liquidator has *both* the right to sue and the right to recover even though the recovery is on behalf of the company.

45. The second class are the voidable transaction claims which are quite different. Section 588FF relevantly says:

Courts may make orders about voidable transactions

(1) Where, on the application of a company's liquidator, a court is satisfied that a transaction of the company is voidable because of section 588FE, the court may make one or more of the following orders:

(a) an order directing a person to pay to the company an amount equal to some or all of the money that the company has paid under the transaction;

(b) an order directing a person to transfer to the company property that the company has transferred under the transaction;

46. In other words, the "right to sue" that the liquidator is given, is only the right to "apply". It does not include any right to recover. If the liquidator's application is successful then the Court may make orders which benefit the company. But the company has no right

of its own to apply for those orders, nor does it have any "right" of recovery. This issue is potentially significant.

The need for notice under section 12 of the Conveyancing Act (NSW) or interstate equivalents

47. Equity was always quite open to recognising the assignment of rights even on an informal basis, so long as the core element of intention by the assignor, the existence of the right in question and certainty what it compromised, and the identity of the assignor could be ascertained.[21] However, the common law did not recognise the assignment of chose in action. It was not until the *Judicature Act* reforms of the 1870s that a statutory solution was set up which meant that, subject to certain requirements of form, equitable assignments of chose in action to be converted into assignments recognised at common law. Section 12 of the *Conveyancing Act* is the local section which performs this function but all States and Territories have like provisions.

48. Section 12 is in the following terms:

> "Any absolute assignment by writing under the hand of the assignor (not purporting to be by way of charge only) of any debt or other legal chose in action, of which express notice in writing has been given to the debtor, trustee, or other person from whom the assignor would have been entitled to receive or claim such debt or chose in action, shall be, and be deemed to have been effectual in law (subject to all equities which would have been entitled to priority over the right of the assignee if this Act had not passed) to pass and transfer the legal right to such debt or chose in action from the date of such notice, and all legal and other remedies for the same, and the power to give a good discharge for the same without the concurrence of the assignor."

49. What section 12 means, is that if you want to obtain a right "effectual in law… to pass and transfer the legal right to such debt or chose in action" as opposed to only effectual in equity, then the assignment you are dealing with must have certain qualities First, it must be "absolute" meaning there cannot be an assignment of part of a chose in action nor can the assignor retain any rights in respect of the chose itself,[22] second it must be "in writing" and third the writing must be signed by the assignor. In practice assignment is almost always done by way of deed because it satisfies the second and third requirements and, at least a common law, avoids issues of consideration.

50. Note that section 12 provides that the deeming does not occur unless notice is given, and that it only occurs "from the date of such notice". Until then, the assignment is only effective in equity.[23]

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[21] Edelman J, Elliot S, *Two Conceptions of Equitable Assignment,* Paper presented to the Current Legal Issues Seminar Series 2013, Banco Court, Supreme Court of Queensland, 6 June 2013, p.6, noting that these requirements are not unsurprisingly also the three certainties.
[22] *Claudio Grizonic v Suzanne Ranken Suttor& ors; Dawn Wade v Suzanne Ranken Suttor* [2011] NSWSC 471 at [20]
[23] *Norman v Federal Commissioner of Taxation* [1963] HCA 21; (1963) 109 CLR 9 at 28-9; [1963] HCA 21; [1964] ALR 131 at 147-8; [1963] HCA 21 at [9] per Windeyer J

51. The section itself does not prescribe a fix form of notice, other than that it "express" and in writing and signed by the assignor[24] The case law regarding what constitutes effective notice, with the older case law taking a much stricter view of what was required, and going so far as to hold the notice must be "strictly accurate" especially as to the date of the assignment[25]. However, more recent case law appears to take a less strict approach by reference back to the words of the section itself, so long as the notice "does not mislead".[26]

52. Importantly, and consistent with common sense, the assignee takes the rights subject to all rights of set-off, counterclaims and all defences to which the potential defendant is otherwise entitled to,[27] so assignees be careful to consider what those might be.

53. Even though the rights conferred on a liquidator which are being assigned are rights conferred by a Federal statute, section 79(3)(b) of the *Judiciary Act* means that the requirements of section 12 should be complied within before the assignee brings the suit.

54. It is also worth noting that section 12 does not say who must give the notice, merely that notice must be given. The case law indicates it may be given by the assignor or the assignee.[28] Nor is it fatal to a suit erroneously commenced before notice is given, and importantly, section 12 does not say that the notice needs to come from the assignor. As to timing in *Assignments of Choses in Action in Australia* the learned author said:

> "67 Time for giving notice - The statutory provisions prescribe no specific time limit within which notice may be given by any particular person. Notice may be given **even after the death of an assignor**..., or after the death of a deceased assignee..., although no notice has been given by him or by the original or any intermediate assignee.... The debtor or fund holder must of course receive notice before payment by him..., or before action brought by the assignee (Cf. *Holt v. Heatherfield Trust, Ltd*., [1942] 2 KB. 1, at pp. 4, 5-6, and McIntosh v. Zhuzhou (1931), 46 CLR. 494, at pp. 514-5. See also *Re Westerton, Public Trustee v Gray*, [1919] 2 Ch. 104, at p. 111.)."

[Emphasis added]

55. However, even if proceedings are brought by an assignee before notice is given, there remains an argument that this is not fatal. In *Treadwell v Hickey* [2009] NSWSC 1395, Barrett J at [98] said:

> "[98] The decided cases…thus make it clear that an action commenced by an assignee before the giving of notice to the debtor or other person bound - that

[24] *William Brandt's Sons & Co v Dunlop Rubber Company Limited* [1905] AC 454
[25] *WF Harrison & Co Ltd v Burke* [1956] 2 All ER 169; *International Leasing Corporation (Vic) Ltd v Aiken* [1967] 2 NSWR 427
[26] *Claudio Grizonic v Suzanne Ranken Suttor & ors; Dawn Wade v Suzanne Ranken Suttor* [2011] NSWSC 471at [25]
[27] *Roxburghe v Cox* (1881) 17 Ch D 520 at 526.
[28] *Anning v Anning* (1907) 4 CLR 1049 at 514-515.

> is, an action commenced by a mere equitable assignee of a legal chose in action - is not a nullity or liable to be struck out or dismissed out of hand. But such an action will not be an appropriate vehicle for the ultimate recovery of a remedy at law unless and until the assignor who is alone entitled to sue at law is a party. By joining the assignor at a later stage ("in due course", to use Viscount Cave's words), the mere equitable assignee by whom the action was initiated makes that existing action a means of obtaining the common law remedy. The action attains that quality because the joinder ensures that the assignor is privy to the eventual judgment and thereby disabled from afterwards asserting the same cause of action against the defendant. It is because the assignor is a party when judgment is ordered that the possibility of double recovery is forestalled. It is beside the point that the assignor was not a party when the equitable assignee acted alone to initiate the proceedings or at any other time before judgment."

56. In terms of the assignment of a voidable transaction, section 12 has two potential applications. First, for an assignment of the liquidator's personal right to apply under section 588FF to be effective in law, the assignment itself must comply with section 12, and express written notice must be given to the prospective defendant if the assignee wishes to sue. Of course, if the assignee is the prospective defendant, the notice becomes otiose. Those assignments are now considered

Assignment by the liquidator

57. As noted in the proposal paper, prior to the insertion of s 100-5, there were doubts as to whether a liquidator's right to apply under section 588FF could be assigned because the Act conferred it on the liquidator personally. Moreover, even at general law there was disagreement whether a bare right to sue was assignable for policy reasons, and whether, if it could not be assigned it was even property.

58. At least with respect to the liquidator's ability to assign those doubts have been now laid to rest by section 100-5.

59. Whether a potential assignee of a voidable transaction claim needs to obtain any more than an assignment of the liquidator's right to apply depends upon who the assignee is. If the potential assignee is the *target* of the potential claim then their aim is simply to make sure the claim never proceeds, which means that owning to apply for relief is enough.

60. However, if the assignee is looking to run the claim, then the assignee will want more than just the right to apply, they will also want to make sure that they get the "fruits" of such claim and it is then that things become more complicated.

Assignment by the Company

61. As noted above in terms of a voidable transaction claim, the company is merely a passive player with no rights to sue. A chose in action is regarded today as personal

right of property.[29] But whilst a company might hope or expect that ultimately the Court will make orders in its favour, it has no ability to apply for those orders or otherwise enforce that the Court does so. In other words, before judgment the company has no rights, and it has no present property to assign.

62. For this reason, what a potential assignee is taking when it purposes to take an assignment of the any money or other benefit which the Court ultimately orders in favour of the company is not an assignment of existing property but of a "mere expectancy", or of "future property".[30]

63. In *Norman v FCT*[31] Windeyer J explained the issue as follows:

> "As it is impossible for anyone to own something that does not exist, it is impossible for anyone to make a present gift of such a thing to another person, however sure he may be that it will come into existence and will then be his to give. He can, of course, promise that when the thing is his he will make it over to the intended donee. But in the meantime, he may change his mind and when the time comes refuse to carry out his promise, even though it were by deed. A court of law could not compel him to perform it. A court of equity would not. Courts of equity never had the objections to all agreements about future interests that, until the seventeenth century, were deeply rooted in the common law. Equity did not share the view that such agreements were void on the ground of maintenance. But things not yet in existence could only be the subject of agreement, not of present disposition. And, in relation to promises and agreements, equity has been faithful to its maxim that it does not come to the aid of volunteers. For equity, a deed does not make good a want of consideration. (at p24)
>
> If we turn from attempted gifts of future property to purported dispositions of it for value, the picture changes completely. The common law objection remains. **But in equity a would-be present assignment of something to be acquired in the future is, when made for value, construed as an agreement to assign the thing when it is acquired**. A court of equity will ensure that the would-be assignor performs this agreement, his conscience being bound by the consideration. The purported assignee **thus gets an equitable interest in the property immediately the legal ownership of it is acquired by the assignor, assuming it to have been sufficiently described to be then identifiable.** The prospective interest of the assignee is in the meantime protected by equity… "And so", to use Maitland's words, "lawyers easily slipped into the way of saying that inequity one could make an assignment of goods hereafter to be acquired though one could not do so at law. This was a compendious way of putting the matter and was not likely to deceive any equity lawyer".
>
> [Emphasis added]

64. In *Palette Shoes Pty Ltd v Krohn* (1937) 58 CLR 1 at 27, Dixon J explained the process as follows:

[29] Tolhurst, G, *The Assignment of Contractual Rights,* Hart Publishing, 2nd ed, 2016 at [2.02] & [2.05] citing *Torkington v Magee* [1902] KB 427 at 430 per Channell J.
[30] For discussion see *Meagher, Gummow & Lehane* at [6-190]
[31] *Norman v Federal Commissioner of Taxation* [1963] HCA 21; (1963) 109 CLR 9

"although the matter rests primarily in contract, the prospective right in property which the assignee obtains is a higher right than the right to have specific performance of a contract, and it may survive the assignor's bankruptcy, because it attaches without more *eo instanti* when the property arises and gives the assignee an equitable interest therein."

65. In other words, even though the making of orders in its favour, there is no property to assign, if value is given, equity regarded this as an enforceable promise that if the expected property ever comes into existence that it would immediately be assigned to the assignee. Thus, the moment that the Court makes orders in favour of the company an equitable interest attaches to them. In *Bakewell v Deputy Commissioner of Taxation*[32] (***Bakewell***) Starke J, described this "interest" as being "an equitable assignment or charge".

66. This gives rise to some interesting issues for voidable transaction claims.

67. The first is that if an assignment of future property by the company is made, that the assignment must be "for value" of can section 12 of the *Conveyancing Act* overcome this? According to J.G. Starke in *Assignment of Choses of Action in Australia:*

[58] Consideration unnecessary – Consideration is unnecessary under the statutory provisions, so that a voluntary assignment is statutorily valid. Even if it be such a voluntary assignment as is not enforceable in equity by the assignee against the assignor, the debtor…cannot set this up as a defence to the proceedings by the assignee."

68. Second, is whether, since the agreement which is, in effect, a promise to assign in the future if property comes into existence, an agreement which needs approval under section 477(2B)? Based on the case law, the answer appears to be no, since even though theoretically the fulfilment of the promise takes place at the moment the property exists, the Court will treat that assignment has having come into effect at the time of the agreement to sign,[33] however there may be still an argument that the "term" of the agreement to assign nevertheless extends beyond 3 months or whether it is the "compromise" of a debt above the prescribed limit.

69. Third, from the point of view of giving notice under section 12 of the *Conveyancing Act*, that notice is effective before the relevant property even exists? It may be, that on the same basis that assignment is regarded as having come into effect from the date of the promise to assign that the notice can be served as soon as the promise to assign is made, however the alternative position would be that it is not effective until the property exists and so needs to be served after any orders in the company's favour are made.

70. Fourth, given that Starke J in *Bakewell* said the interest which arises is an equitable assignment *or* charge, which is it? Could it be both?

[32] (1937) 58 CLR 743 at 761-2
[33] *Puntoriero v Nickpack Pty Ltd* [1992] FCA 257

71. Fifth, if there is some potential issues about the validity of the assignment which might involve the company, should the assignee consider bargaining for some ability to ensure that the company is not deregistered prior to the assignee receiving the benefit of orders made in the company's favour?

72. Sixth, given that the company is promising to assign rights to future property in advance, does that assignment still occur even if the company is, by that time, deregistered? The case law suggests that it should, although the proposition appears untested. As Dixon J said, the assignment "may" survive bankruptcy and the case law indicates that notice of assignment can be given even after the assignor has died.[34]

73. Seventh, a potential assignee will need to be alive to the fact that that even though they may take the rights of the company to a voidable transaction claim, section 553C means where there are mutual dealings, a creditor is entitled to have debts the company owes it, set off against debts it owes the company meaning that the expected returns to the company (and the assignee) maybe less than expected.[35] These would include claim against the company prior to the date of assignment.[36]

The notice requirements of section 100-5

74. Beyond specifying that the notice of proposed assigned must be given "before" the assignment and that it must be "written" Section 100-5 gives no guidance as to the notice requirements.

75. The following issues seem likely to arise:

    (a) what level of detail must the notice give?

    (b) how long before must it be given?

    (c) must is specify which rights to sue are being or have been assigned?

    (d) must it specify against whom those rights operate?

    (e) must it specify what, if any consideration is being received?

76. As for the other questions neither the Proposal Paper, nor the Explanatory Memorandum nor the Act provides any guidance, but a useful starting point might be, what was the intention of Parliament in requiring the giving of written notice in any event? Given that a liquidator is not required to give notice to creditors that he or she wishes to, assign rights to sue which the company owns why would Parliament require notification of the assignment of these rights?

77. There seem to be at least three possible answers. One might be that the creditors are potential purchasers of these rights and might wish to bid for them but if that were correct why aren't liquidators required to give notice of the assignment of the company's other claims to the creditors as well?

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[34] *Anning v Anning* (1907) 4 CLR 1049 at 1059
[35] *Morton v Rexel Electrical Supplies Pty Ltd* [2015] QDC 49
[36] Starke, J.G. *Assignment of Chose in Action in Australia,* Butterworths, 1972 at [41]

78. Second, perhaps Parliament considered that the rights to sue conferred on a liquidator had special characteristics that meant that their assignment would be of importance to creditors. This might be because creditors are the focus of unfair preference claims and may wish to object to their assignment, or because the creditors may object to rights such as the right to sue for insolvent trading passing out of the hands of an insolvency practitioner whose behaviour is highly regulated, and into the hands of an assignee who is not, however this is mere speculation.

79. A third possibility is that the notice provision is just an example of a general trend toward more transparency and involvement of creditors in the latest round of reforms, and that the notice provisions are simply part of that trend of keeping creditors more informed. Given the lack of an explanation for the subsection, this reason seems most plausible. If that be so, then presumably the reason for the giving of the notice to creditors is so that they can request more information from the liquidator or they can object to the proposed decision or potentially replace the liquidator.

80. If that is correct, it implies certain things about the notice. First, would to be given to the creditors with sufficient time for them to consider it and formulate an objection to the proposed transaction or take other action as they think fit.

81. Second, that it is arguable that the notice could contain either very little information, on the basis that this merely alerts creditors who may request further information if they wish to, or alternatively that it needs to contain sufficient information to enable a creditor to determine whether they wish to object to the proposal or take other action.

82. At one end of the spectrum would be a notice that simply said: "The liquidators propose to assign rights to sue conferred upon them by the Corporations Act. Please contact the liquidators if you require further information."

83. At the other end would be a notice which said something like: "On [date] the liquidators propose to assign to Jane Smith, for consideration of $10,000 the right to sue John Doe under section 588FF of the *Corporations Act* in respect of an alleged unfair preference received by him in the amount of $350,000".

84. Arguably the first notice is so vague that it gives the creditors no real ability to understand what is occurring, to the extent it is insufficient to qualify as a notice. The second is so specific, that it when John Doe receives it, he will be able to infer that the liquidator considers the claim against him is weak thereby devaluing the assignee's ability to compromise the claim for a reasonable sum. Or, on the flip side, it might spur John Smith to offer the liquidator $20,000 for the rights to sue him, thereby protecting himself from the risk of litigation.

85. In the end, what is likely to constitute sufficient notice depends on the circumstances of the case. In considering the requirements of various types of unilateral notices *Robinson v Becata Pty Limited* [2004] NSWSC 310, Campbell JA said:

> "There are significant differences between the various types of unilateral notice which I have been considering…however, a common theme runs through the cases

> concerning these various types of unilateral notice, to do with the approach taken to construing the notices. For all of them, an effective notice is one which conveys its message (whatever that message might be) clearly and distinctly to a reasonable reader in the position of the recipient of the notice. Being “in the position of the recipient” involves, in particular, having the knowledge of the circumstances surrounding the transaction in which the notice is given which the recipient has or ought to have.”

86. Until these issues surrounding the adequacy of these notices is resolved by caselaw, or perhaps by promulgation of a prescribed form, liquidators will need to give careful consideration to what constitutes appropriate notice in the circumstances.

Approval by the Court after proceedings have commenced

87. As section 100-5(2) makes clear, a claim which has already commenced cannot be assigned without approval of the Court. Presumably this approval will be sought from the Court in the same way that judicial advice is currently sought by liquidators.

88. Given that the case in question would already be underway, it is unlikely to be appropriate that the application be made within those proceedings itself, since it may well be necessary to disclose opinions as to success and other privileged information. On the other hand, it seems likely that once approval is obtained it will need to be presented to the Court in the existing matter as a basis for the liquidator to be replaced by the assignee as the proper applicant.

89. In terms of the criteria that a Court would apply in considering whether assignment should be approved it is to be expected that, consistent with the Court’s general approach, the Court would defer on questions of commerciality to the liquidator, however the Court would also want to be satisfied that the assignment of the claim is in the interests of the creditors as a whole. Presumably approval is required from the court on the basis that the creditors may be interested in the outcome, given that some or all of them may be defendants to the action already underway.

Information and access to books and records?

90. Unlike a liquidator an assignee of the liquidator’s right to apply under section 588FF does not have the liquidator’s automatic powers to conduct public examination, the right to access the books and is not owed any duty of assistance by directors or officers.

91. Therefore, as a practical issue, assignees who purchase a claim with a view to running it will want to be able to obtain and possibly the liquidator’s assistance both assess the claim’s prospects, assess its value, draft the pleadings and adduce the evidence. In terms of public examinations, it may be that ASIC will be prepared to assist assignees to actions by granting them the status of “eligible applicants” for such examinations.

92. If a liquidator has already done examination and obtained documents, the question of whether the *Harman* undertaking applies to those documents should be considered

before they are disclosed,[37] and for the avoidance of problems it should be remembered also that section 597(14A) (b) will enable a third party to get access to the "records of the examination" upon payment of a fee.

93. As with the sale of all claims, a liquidator assigning a voidable transaction claim will need to consider what level of ongoing assistance, if any, which he or she is prepared to give to the incoming assignee and whether any agreement to provide assistance extends beyond 3 months and requires approval.

In whose name is the assigned claim brought?

94. Since after assignment, the reference to a liquidator in section 588FF become a reference to the assignee, the claim thereafter should be brought in the name of the assignee, or if it has already commenced, the name of the applicant should be amended to the name of the assignee.

What about claims that are vexatious or hopeless?

95. It has long been held that a liquidator should not assign claims which are hopeless or have no reasonable prospects of success. In *Citicorp Australia Ltd & Ors v Official Trustee in Bankruptcy & Anor* [1996] FCA 1115, a Full Court of the Federal Court of Australia, having reviewed various authorities on assignment of causes of action in an insolvency context said:

> "The foregoing authorities do not deny that in a case where it is clear that the claim sought to be pursued by the bankrupt or other proposed assignee is frivolous or vexatious, the trustee or the court should not allow the assignment to occur. A claim with no reasonable prospect of success would be a frivolous one, and the prosecution of such a claim would be vexatious. As earlier noted, in most cases it will not be clear that an alleged claim has no reasonable prospect of success. However, when a clear case arises, the trustee as an officer of the Court, and the Court itself, in the public interest, should not allow the assignment to occur, even where an immediate sum of money is offered as consideration that would benefit the estate of the bankrupt."

96. However, as Brereton J noted in *Re SCW Pty Ltd* [2013] NSWSC 302 (***Re SCW****)* at [15]:

> "…where a creditor or intervening party contends that an assignment should not be authorised because the proposed claim has no prospects of success, it is for that party to demonstrate the absence of any prospect of success."

Does the liquidator need to assess the merits of a claim before assigning it?

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[37] [1983] 1 AC 280; *Hearne v Street* (2008) 235 CLR 125 at [107]-[108]. The principle being that Information that is not in the public domain and was obtained by discovery or subpoena, or a public examination process cannot be used for a collateral or ulterior purpose unrelated to the proceedings in which the information was obtained, although in general terms it is accepted that information obtained involuntarily obtained by a liquidator in a public examination setting can be used in subsequent proceedings, it is not clear that this applies to an assignee.

97. In general terms, if funds are available a liquidator should normally assess, at least on some basis, the value of a claim or potential claim before assigning it so that the liquidator can assess whether the price being received for it is reasonable in the circumstances. However, in many circumstances an absence of funding may mean that a liquidator is not able to make any real assessment of the value of a claim before assigning it.

98. In *Re SCW* as the liquidator had assessed certain claims as hopeless but a purchaser had offered $100,000 for them and furnished an opinion of senior counsel that they were not hopeless. The liquidators sought judicial advice that they were justified in *not* assigning the claims. Brereton J, said:

> "…it was said that the proposal would involve the assignment of claims, including claims against third parties that had not been investigated or valued. As was also pointed out in *Citicorp Australia v Official Trustee in Bankruptcy* (1996) 141 ALR 667 the power of sale of a trustee in bankruptcy or a Liquidator is not circumscribed by a duty to first ascertain that the claim is one with a reasonable prospect of success, and to require the trustee to investigate the prospects would be inconsistent with the position that the trustee might decide to sell what was the estate without funds or to hasten the winding up of the insolvency. See also *Seear v Lawson* (1880) 15 CD 426; *Stein v Blake* supra; and *Ramsay v Hartley* (1997) 1 WLR 686. Again, the fact that the Liquidator is not able to and has not valued the claims in question is, it seems to me, quite beside the point in the context that those claims will, if not assigned under the proposal, otherwise generate no value at all for the company in liquidation."

[Emphasis added]

99. The upshot of this is that, whilst a liquidator is not obliged to investigate the value of a claim or investigate its prospects of success before assignment, if the claim is, in fact hopeless, then the transfer can be challenged, notwithstanding that the challenger bears the onus of proof. Accordingly, a liquidator assigning a cause of action should consider whether it is feasible to obtain an indemnity from the assignee in the event that the transfer is subsequently challenged.

What is the correct price for the assignment?

100. This issue is sufficiently complex to warrant a paper of its own, however in principle, there is no reason why the approach to the valuation of a voidable transaction claim should be different from the valuation of other claims which liquidators have always been able to assign. Ultimately, although the liquidator holds the right to sue, the right is for the benefit of the company and it would have been the company which would receive the ultimate benefit of any others

101. Having said that, the value of a claim to a company is influenced by the ability of the liquidator to run it to completion. Whilst in hindsight a creditor may challenge the fact that what turned out to be a very successful claim was assigned at a low price to an assignee, as Brereton J noted in *Re SCW,* if the liquidator cannot run the claim, then

it has no value to the company and so it's sale at any price is to the advantage of creditors.

Conclusions

102. The growing trend of giving creditors more transparency as to the conduct of the liquidation together, with the ready availability of avenues for creditors to seek review of the liquidator's decisions have, unfortunately, coincided with the passage of section 100-5 which throws up various issues upon which there is no bright line. Until case law explores these issues, liquidators will need to carefully consider their actions, and do their best to ensure that, if their decisions are reviewed, that they are able to justify the decisions they have made.