

Mr Henry Carr  
Director  
Fair Entitlements Guarantee Recovery Team  
Workplace Relations Programmes Group  
The Department of Employment  
12 Mort Street  
CANBERRA ACT 2601  
Via email: [ImprovingFEG@employment.gov.au](mailto:ImprovingFEG@employment.gov.au)

16 June 2017

Dear Mr Carr,

**Consultations Paper on “Reforms to address corporate misuse of the Fair Entitlements Guarantee Scheme”**

This is a submission by the Insolvency and Reconstruction Committee of the Business Law Section of the Law Council of Australia (**Committee**) in response to the consultation paper dated May 2017 on “Reforms to address corporate misuse of the Fair Entitlements Guarantee scheme” (**Consultation Paper**).

**Summary**

The Committee generally supports measures to address potential abuse of the Fair Entitlements Guarantee Scheme (**FEG scheme**).

However, the Committee suggests it would be helpful to better articulate the sharp corporate practices that the draft amendments seek to address. The broad example listed at sub-paragraph 3.2(i) on page 4 of the Consultation Paper is vague. There are already legal solutions available to address the practices set out at sub-paragraphs (ii), (iii) and (iv) on page 5 of the Consultation Paper.

As explained below, the Committee supports a number of the proposed measures. However, the Committee asks that the legislative drafters be clear in the behaviour that is sought to be addressed and consider if and why existing laws and measures are inadequate.

The Committee's response to the proposals set out in the Consultation Paper are detailed below.

### **Should Part 5.8A be amended?**

The Committee supports amendment to Part 5.8A.

The Committee is concerned that, even on its current reading, Part 5.8A could be interpreted widely to include prohibitions on deeds of company arrangement and schemes of arrangement. The Committee submits that there should be a carve out of deeds of company arrangement and schemes of arrangement because there is already some protection of employees, namely:

- (a) in the case of a deed of company arrangement, eligible employee creditors are given priority unless they pass a resolution otherwise or the Court orders otherwise (section 444DA of the *Corporations Act*); and
- (b) a scheme of arrangement is subject to Court approval.

This carve out becomes particularly important if Part 5.8A is amended as proposed.

### **Submissions on the options set out in the Consultation Paper**

#### Option 1: Extend the fault element in section 596AB to include recklessness and increase the maximum penalty

The Committee is not adverse to the proposed amendment to include recklessness. However, the Committee notes that the element of recklessness is already present in a number of offences under the *Criminal Code (Cth)* and yet it is rarely applied. The Committee therefore questions whether this amendment would achieve the stated purpose.

Given that the current provision is seemingly ineffective<sup>1</sup> the Committee cannot comment upon whether an increase in penalty will achieve the stated purpose. Overall, the Committee supports the introduction of a civil penalty provision as a measure more likely to achieve the stated objectives.

#### Option 2: Introduce a separate civil penalty provision with an objective test

The *Corporations Act* contains a number of civil penalty provisions to prohibit certain behaviour (for example, sections 180 to 183 regarding directors' duties). The introduction of a civil penalty provision to address abuse of the FEG scheme is in keeping with the current framework for addressing particular behaviour. However, as a general comment, the effectiveness of any civil penalty provision does depend on whether those targeted have any assets.

Of the two proposed options, the Committee would prefer the first. However, it is unclear exactly what conduct this would address. The example given on page 11 of the Consultation Paper appears to be one that could be addressed by the current uncommercial transaction provisions (ss. 588FB and 588FC of the *Corporations Act*).

---

<sup>1</sup> Page 8 of the Consultation Paper

The second option provides too much uncertainty as to how a Court would exercise its discretion when looking at conduct in hindsight. If the application of the provision is uncertain then it might not provide the desired outcome of preventing particular behaviour in relation to abuse of the FEG scheme. Further, the first factor suggests that there should be an analysis of the benefit or detriment “to the company” in entering the agreement or transaction whereas the analysis should be of the benefit or detriment on the company’s ability to meet its obligation for employee entitlements. (An agreement might still be of benefit to the company while sacrificing payment of employee entitlements.) Rather than electing either option 2A or option 2B, the Committee suggests consideration of a provision that echoes the objective test currently set out in section 588FB of the *Corporations Act*. The provision would prohibit any agreement or transaction of the type stated in section 596AB (a) or (b) if a reasonable person in the company’s circumstances would know, or would be expected to have known in the circumstances that such agreement or transaction would cause loss or damage to employees having regard to:

- (a) the benefits (if any) of the transactions on the company’s ability to meet its employee entitlement obligations;
- (b) the detriment of the transactions to the company’s ability to meet its employee entitlement obligations; and
- (c) any legitimate purposes to the business in entering into it.

Unlike for sections 588FB, 588FC and 588FE, the new proposed provision could operate even if the company is solvent at the time of the agreement or transaction.

#### Option 3: Expand the parties who may initiate civil action

The Committee supports this proposal.

#### Option 4: Addressing other issues with the Part’s drafting

The new provisions should not be drafted so broadly that they inadvertently capture agreements or transactions that are not intended to be captured.

For example, financiers generally draft their security documents to secure as much of the company’s property as possible. With the introduction of the *Personal Property Securities Act* a financier can, in effect, elect whether an asset that would traditionally be a “floating charge” is a circulating security interest (and subject to the priority of employees’ claims in section 561 of the *Corporations Act*) or a non-circulating security interest simply by the amount of control it exerts over the use of the assets.<sup>2</sup> Arguably, if the amendments are drafted too widely, either the entry into the security documentation or the financier’s conduct in making such an election, could be caught. As there is no suggestion in the Consultation Paper that such activities would constitute a sharp practice that needs to be addressed, the Committee assumes that such activities are not intending to be caught.

---

<sup>2</sup> s 340 *Personal Property Securities Act 2009* (Cth) and *Re Amerind Pty Ltd (Receivers and Managers Apptd) (In Liq)* [2017] VSC 127.

The Committee further notes that any amendments should be drafted with a clear view of the behaviours that fall outside acceptable practice. The Consultation Paper refers to “sharp practices” rather than illegal activity so there needs to be a clear articulation of the specific behaviour that the amendments will address. Further, a number of examples of sharp practices or poor behaviour outlined in the Consultation Paper could be addressed under the current legal framework (for example, through investigation and discipline of registered liquidators or by action for breaches of directors’ duties).

The Committee shares the underlying concern about unregulated “pre-insolvency advisors” facilitating or orchestrating phoenix activity. However, the Consultation Paper appears to focus on the outcome of improper phoenix activity, rather than the transaction itself. In order to be effective, any new provisions will need to focus on the agreements and transactions that will be targeted. The danger is that this focus is not clear from the proposed options.

#### Option 5: Corporate groups to provide a contribution equivalent to any unpaid employee entitlements in some limited circumstances

The Committee considers that the proposed approach has the following risks and drawbacks:

1. The proposed criteria are vague and subjective and may lead to uncertainty on the part of both employees post appointment and directors pre-appointment who are considering corporate structure and risk issues;
2. The proposal would require a liquidator of an insolvent employee entity to either obtain funding or dissipate the limited funds available in the liquidation, to prepare the evidence required to support a contribution order and run a contested proceeding to obtain a contribution order.

While, the Committee is not aware of any statistics or evidence from New Zealand and Ireland to confirm that this measure would work, the Committee is concerned that this proposal may not ultimately address the issue identified in section 6. If this proposed measure is to be introduced, the Committee submits that section 48(2) of the *Corporations Act* should not apply. That sub section suggests that a trustee subsidiary company would not be caught.<sup>3</sup>

Another option that the Committee considers should be explored is the approach used in *Workplace Injury Rehabilitation and Compensation Act 2013* (Vic) (ss 430-432) and *Payroll Tax Act 2007* (Vic) (ss67-81) which impose joint and several liability automatically across a corporate group for employee related taxes and charges if certain criteria are satisfied. Under this legislation, related entities (within the meaning of section 50 of the *Corporations Act*), entities with (amongst other things) a common director, or entities carrying on the same enterprise are jointly and severally liable for the employee related liabilities of the employer entity within the group. An entity within the corporate group can apply to be administratively excluded from this joint and several liability, if the authority is satisfied of certain matters (such as not carrying on the same business) that make it just and equitable for an entity to be excluded from the group. The Committee notes that these existing provisions deal with debts due to a state government, rather than an entity within a corporate group, so the framework will necessarily need to be adapted such that the

---

<sup>3</sup> The Committee notes that this is currently an issue with the operation of section 588V of the *Corporations Act*.

other entities within the corporate group are only liable on certain trigger events (possibly the insolvency of the employer).

The Committee considers that the approach of legislating automatic joint and several liability within a corporate group for employee entitlements when certain criteria are satisfied has the following benefits:

1. The business community can have certainty as to what liabilities entities in the corporate group may be liable for at the outset, and plan for these appropriately, including making exemption applications if appropriate; and
2. A liquidator of the employer entity, and ultimately the priority creditors themselves, will not bear the significant evidentiary and costs burden of obtaining a contribution order after the employer has become insolvent.

#### Option 6: Specific FEG sanctions for directors in Part 2D.6

The Committee submits that the current disqualification criteria is adequate to address the behaviour outlined and should be simpler to prove than the proposed criteria. The proposed criteria does not seem to add a set of behaviours that would not otherwise be caught by other existing provisions.

In particular, the following provisions would appear to allow disqualification where a director contravenes provisions relating to the FEG scheme:

- (a) section 206C of the *Corporations Act* - where there is a breach of a civil penalty provision and the Court is satisfied that the disqualification is justified;
- (b) section 206E – where the person has at least twice contravened the *Corporations Act* while an officer and the Court is satisfied that the disqualification is justified;
- (c) section 206F – where, in the previous 7 years, the person has been an officer of 2 or more corporations that were wound up and where the liquidator lodged a report under section 533(1) (noting that such a report is lodged where the company may be unable to pay its unsecured creditors more than 50 cents in the dollar).

Subject to specifying the particular offences, the Committee generally agrees with the proposal to extend the current provisions to cover company offences for employee entitlements-related offences prescribed by legislation other than under the *Corporations Act*.

#### Option 7: Reform of the law regarding trust assets where an insolvent company is a corporate trustee

There is a myriad of issues that arise on the insolvency of trustee companies and the Committee advocates for reform to deal with all those issues.

The Committee refers to and attaches a paper it has drafted to deal with issues arising from the use of trust structures more generally. In particular, the Committee refers to paragraphs 55 to 62 and 73(e) in response to the specific questions raised in the Consultation Paper.

In summary, the Committee supports the proposal to apply the statutory order of priorities to the distribution of the trust assets of an insolvent trading trust.

Further, and as explained in the attached paper, the Committee supports:

- (a) consideration of the Australian Law Reform Commissions' recommendations in the 1998 Harmer Report<sup>4</sup>;
- (b) clarification of a liquidator's duties and powers when appointed to a trustee company;
- (c) extending the definition of "property" in the *Corporations Act* to include trust assets;
- (d) allowing liquidators to claim remuneration and expenses out of trust assets;
- (e) clarification to the effect that a former trustee can bring an action for possession of trust property; and
- (f) clarification that the claw back provisions in the *Corporations Act* apply to transactions involving trust assets.

The Committee notes that trust law is generally the purview of common law and each State and Territory *Trustee Act*. Therefore, there may be a need to either uniformly amend the various *Trustee Acts* or reach agreement with the States for a referral of their powers in relation to trusts in this particular area.

#### Option 8: Clarify the priority of employee entitlements under section 433 and 561 of the Corporations Act and align the sections

The Committee agrees generally with the need to improve certainty by amending sections 433 and 561 of the *Corporations Act*.

The Committee notes the proposal to maintain priority for the liquidator's costs associated with the realisation of the relevant assets. The Committee supports maintaining this priority and extending it to include:

1. the costs recoverable under the *Re Universal Distributing*<sup>5</sup> principle, namely all costs related to the protection, preservation and realisation of the assets; and
2. the liquidator's costs of complying with sections 433 and 561. These would include the cost of determining whether those sections apply, to which assets they apply and the priority claims made under those sections (ie. whether there is a priority and the quantum of the priority claim).

---

<sup>4</sup> Australian Law Reform Commission 'General Insolvency Inquiry' [1988] ALRC 45, 149 – 159. (See also paragraph 12 of the attached paper.)

<sup>5</sup> *Re Universal Distributing Co Ltd (in liq)* (1933) 48 CLR 171

We look forward to participating in the stakeholder meetings to further discussing the proposals raised in the Consultation Paper. If you have any questions in relation to this submission, in the first instance please contact the Committee Chair, Victoria Butler, on 08-9426 6694 or via email: [vbutler@jacmac.com.au](mailto:vbutler@jacmac.com.au)

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Teresa Dyson', written in a cursive style.

**Teresa Dyson, Chair**  
Business Law Section

Enc.

**INSOLVENCY AND RECONSTRUCTION LAW COMMITTEE  
BUSINESS LAW SECTION, LAW COUNCIL OF AUSTRALIA**

**LAW REFORM PROPOSALS - TRUSTS**

**Introduction**

Traditionally, trusts were a passive device whereby a person held property for the benefit of another.

There are now many different types of trusts.

Our particular concerns are the problems raised by the widespread use of corporate trustees to operate various forms of trading trusts where:

- (a) the trading activity results in insolvency; and/or
- (b) the rights of the beneficiaries/unitholders/shareholders are unclear.

These issues with trading trusts result in confusion between the application of corporations law, equity, common law and the legislation in the various States dealing with trusts and trustees.

The Law Council in this submission highlights by reference to reported examples, how this confusion is undermining:

- (a) the ability of liquidators to efficiently carry out their duties;
- (b) the protection which the corporations law otherwise confers on creditors; and
- (c) the ability of beneficiaries to effectively protect their interests.

We then put forward suggestions as to appropriate law reform proposals.

We are concerned that absent appropriate law reform, the issues we have identified will continue to create uncertainty and increase costs



to all parties involved in resolving these issues on a case by case basis.

This submission is in two parts.

Part A deals with issues arising where liquidators are appointed to companies that are trustees of trading trusts.

Part B relates to remedies available to beneficiaries where there are disputes between them.

## INDEX

	<b>Topic</b>	<b>Page</b>
PART A	Proposal to clarify the law in respect of liquidators dealing with trust assets	3
I	Summary	3
II	Background	4
III	Typical factual situation	7
IV	Practical difficulties faced by insolvency practitioners	8
V	Effect of replacement of Trustee	11
VI	Liquidator's duties	12
VII	Trustee's right of indemnity and recoupment	13
VIII	Liquidator's remuneration and expenses	21
IX	New Trustee's right to trust assets	23
X	Which creditors are entitled to proceeds of indemnity?	24
XI	Public policy	26
XII	Submission for reform	29
XIII	Recommendation	31
PART B	Remedies available to beneficiaries in dispute	32
I	Recommendation	35

## **PART A**

### **Proposal to clarify the law in respect of liquidators dealing with trust assets**

#### **I. Summary**

1. This submission highlights a number of inconsistencies that exist between the States in respect of their common law, and which result in practical difficulties being faced by liquidators when appointed over companies that act as trustees, when dealing with the assets of those trusts.
2. These inconsistencies are leading to practical difficulties and additional costs being incurred by liquidators winding up companies which act as trustees. As this submission highlights, liquidators are being required to seek directions from the court in circumstances where such directions would not be required had the company not been acting as a trustee. This has the effect of delaying the distribution of assets to creditors and reducing the funds available for such distribution.
3. It is submitted that the current situation cannot be overcome by an appropriate test case being run, as several elements of the disparity relate to inconsistent decisions by State Courts of Appeal particularly in relation to the issue of which creditors are entitled to the proceeds from the right of indemnity, as highlighted in this submission. In order to overcome this difficulty it would require a test case to be taken to the High Court, the costs of which would be excessive in the case of the majority of administrations where these difficulties arise namely where a company acts as trustee of a family discretionary trust.
4. The lack of uniformity in State and Territory legislation, as is highlighted in this submission, also occasions differences as to which assets become vested in any new trustee appointed, and the timing of any vesting.

5. This submission proposes that uniform amendments be made to the Trustee Acts of each State and Territory, or alternatively a referral of power be made to the Commonwealth to allow the passing of legislation that will make certain how a liquidator is to deal with those assets as well as proposing that the rules of the superior courts are changed so as to improve the procedures for liquidators seeking a court's approval to sell assets when that is required.
6. This submission is timely particularly in light of the Australian Government's May 2017 consultation paper titled, "Reforms to address corporate misuse of the Fair Entitlements Guarantee scheme" (**Consultation Paper**), options 7 and 8 of which directly relate to the issues raised in herein.

## II. Background

7. Under the Australian model of federation, jurisdiction with respect to trust law has traditionally vested in the States. This has led to variations in the law existing between States. This in turn affects how trust deeds are interpreted as the ordinary choice of law rules apply to make the laws of the State nominated in the trust deed apply to the interpretation of that trust instrument. Trusts can trade over State boundaries however, and may own real estate in more than one State which may further complicate the choice of law applicable. Some of the practical effects on liquidators of these differences in the law between the States are discussed below.
8. The common law as it exists at present in relation to the interrelationship between insolvency law and trust law varies between States as their courts have found it difficult to grapple with the different underlying public policy considerations that affect this interaction being:-

- (a) The principle of giving a pari passu distribution to creditors of the same class under insolvency law;
  - (b) The fiduciary duty that the trustee has to protect the trust assets and to act in the interests of the beneficiaries;
  - (c) The need for liquidators of corporate trustees to ascertain their right to deal with trust assets and to be able to make this determination efficiently; and
  - (d) The need for courts to ensure that any person appointed to wind up a trustee of a trust (ie: a liquidator or receiver) is properly and reasonably remunerated in order that people will be willing to perform this function.
9. These competing concepts have given rise to a number of conflicting results as courts strive to achieve the best outcome in the relevant circumstances.
10. The common law in relation to trusts does not seek to distinguish between the types of trust that it applies to. Whilst a number of statutory trusts may have special rules or powers given to a court as set out in statute, the common law rules continue to apply to the extent to which such powers or rules are not specified. The common law therefore has to have sufficient flexibility to allow it to cover the different types of trusts, some of which will have little or no documentation that specifies what is to occur if the trust becomes insolvent. The different types of trusts include:
- Statutory Trusts (eg: Superannuation Funds, Managed Investment Schemes, etc);
  - Charitable Trusts;
  - Unit Trusts;
  - Discretionary Trusts;

- Implied Trusts;
- Resulting Trusts;
- Constructive Trusts; and
- Testamentary Trusts.

11. Flexibility is therefore required in any proposed system of regulation governing how these competing concepts are to be dealt with.

12. In 1998 the Australian Law Reform Commission (**the Commission**) in the Harmer Report recommended that:-

- (a) There should be legislative provisions stating that a reference to the business or affairs of a company for the purposes of the operation of the insolvency provisions of the legislation should expressly include a reference to its business or affairs as trustee.
- (b) Any reference in the companies legislation to the property or assets of a company that is being wound up in insolvency should include property and assets held by the company as trustee to the extent that the company is entitled to a charge or other beneficial interest in respect of the property or assets.
- (c) There be a legislative provision which provides that terms or conditions in a trust instrument or agreement that might have the effect of excluding or barring a company from exercising an equitable right against trust property for debts and liabilities properly incurred by the company in the conduct of the trust be void against the liquidator.
- (d) If a company is acting as the trustee of a trust and becomes subject to an application for winding up in insolvency, any provision in the trust instrument allowing for the removal of the company as trustee shall have no effect, subject to any court order.

- (e) Upon the insolvency of a corporate trustee, the exercise of the right of indemnity against both the trust property and beneficiaries may be exercised by the company through its liquidator or administrator on behalf of all trust creditors, subject to any court order.
  - (f) The right of indemnity be extended to include the total costs associated with the winding up of the company.
  - (g) The first priority for payment from the funds received from the right of indemnity is the costs associated with exercising the right to indemnity and then the administration costs of the winding up and then creditors in accordance with the statutory priorities under the companies legislation.
  - (h) The proceeds from the exercise of the right to indemnify should be distributed amongst creditors of the trust that provided the indemnity.<sup>1</sup>
13. None of the above recommendations were implemented.

### **III. Typical factual situation**

14. The typical situation faced by liquidators arises where the company over which they are appointed acts or has previously acted as trustee of a trust, and there are creditors owed monies incurred whilst the company was acting as trustee.
15. The trust deed may contain a clause which automatically removes the trustee upon an insolvency event such as liquidation or voluntary administration. In such circumstances, the company continues to operate as trustee of a bare trust in relation to those assets which remain vested in the trustee.<sup>2</sup> Generally the trustee may then be replaced. Alternatively, nothing further happens in relation to the trust

---

<sup>1</sup> Australian Law Reform Commission 'General Insolvency Inquiry' [1988] ALRC 45, 149 - 159.

<sup>2</sup> *Lewis v Nortex Pty Ltd* (2013) 211 FCR 483, 503-4 [77].

but the original trustee company remains the registered proprietor of any assets held on trust.

16. Where there is no automatic removal clause and the company remains trustee of the trust even though it has been placed into liquidation, the company can rely upon any right of indemnity or power granted to it by the trust deed to access the trust assets to satisfy their right of indemnity.<sup>3</sup>

#### IV. Practical difficulties faced by insolvency practitioners

17. This submission refers to the following issues that tend to arise when a liquidator is appointed to a trustee company in the current context of a lack of certainty or consistency in Australian law.

##### *(a) Power to sell trust assets*

If the trustee company becomes a bare trustee upon the appointment of a liquidator by virtue of an automatic removal clause or a new trustee is being appointed, the question arises as to what powers the liquidator has to retain or sell trust property that remains in his or her possession. Specifically, can a liquidator rely on his or her general power of sale under section 477(2)(c) of the *Corporation Act 2001* (Cth) (**Corporations Act**) to liquidate trust assets, or does the liquidator require court authorisation and/or to be appointed as a receiver of the trust's assets to sell those trust assets? Further, can a receiver or controller within the meaning of the Corporations Act enforce a trustee's right of indemnity?

A further question arises as to whether the right of indemnity falls within the definition of 'property of the company' under Chapter 5 of the Corporations Act? The authorities diverge in this regard. Cases that have considered this include:

---

<sup>3</sup> *Garra Water Investments Pty Ltd (in Liquidation) v Ourback Yard Nursery Pty Ltd* [2012] SASC 11 (26 March 2012) [26].

- *Re Enhill* 1982 VR 561 (**Re Enhill**);
- *Re Suco Gold Pty Ltd Pty Ltd (in Liquidation)* (1983) 33 SASR 99 (**Re Suco Gold**);
- *Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* (2008) 74 NSWLR 550 (**Lemery Holdings**);
- *Apostolou v VA Corporation of Aust Pty Ltd* [2010] FCA 64 (**Apostolou**);
- *Apostolou v VA Corporation of Aust Pty Ltd* [2011] FCAFC 103;
- *Caterpillar Financial Australia Ltd v Ovens Nominees Pty Ltd* [2011] FCA 677 (**Caterpillar Financial**);
- *Prior v Simeon [No 2]* [2011] WASC 61;
- *Re Neeeat Holding (in Liquidation)* [2013] FCA 61 (**Neeeat Holding**); and
- *Re Amerind Pty Ltd (Receivers and Managers appointed) (in Liquidation)* [2017] VSC 127 (**Re Amerind**).

(b) *Distribution of assets*

Questions arising in relation to the distribution of assets include whether trust assets are available for distribution amongst general creditors (ie: both trust and non-trust creditors) or only trust creditors, and whether the statutory priorities under the Corporations Act (including those in relation to employees) apply when there are insufficient funds to pay all the creditors (and if not, what priority is to apply for payment of creditors).

Cases that have considered these matters include:

- *Re Enhill*;
- *Re Suco Gold*;
- *Ramsay v National Australia Bank Ltd* [1998] VR 59;
- *13 Coromandel Place Pty Ltd v CL Custodians Pty Ltd (in Liquidation)* (1998) 30 ASCR 377;
- *Collie v Merlaw Nominees Pty Ltd* (2001) 37 ACSR 361;
- *Commissioner of Taxation v Bruton Holdings Pty Ltd (in Liquidation)* (2008) 173 FCR 472;
- *Caterpillar Financial*;
- *Fletcher, in the matter of Starrit Pty Ltd (in Liquidation)* [2012] FCA 803;
- *Re MF Global Australia Ltd (in Liquidation) (No 2)* [2012] NSWSC 1426 (**Re MF Global**);
- *Agusta Pty Ltd v Provident Capital* [2012] NSWCA 26;
- *Commissioner of Taxation v Fitzroy All Pty Ltd* [2013] WASC 427;
- *Re Independent Contractor Services (Aust) Pty Ltd (No 2)* (2016) NSWSC 106; and
- *Re Amerind*.



(c) *Claw back provisions*

Questions arising in relation to voidable transactions include whether, where a transfer of the trust property occurs prior to the liquidation of the trustee, the provisions of Part 5.7B of the Corporations Act apply to those transactions. This is an issue that has arisen because of the reasoning in *Re Amerind*.

(d) *Payment of a liquidator's remuneration and expenses from trust assets*

This question is related to (b) above insofar as the liquidator may be a creditor of the company, a creditor of the trust, or both.

In the case of trustee companies with insufficient assets (other than trust assets) to meet the liquidator's expenses, clear guidance is needed as to the extent to which a liquidator may apply trust property to meet their remuneration, and the appropriate mechanism for doing so.

Further, if a company acts in more than one capacity (ie: as trustee of a trust as well as in its own capacity, or as a trustee of multiple trusts) to what extent can the trust assets be used to pay the liquidator's remuneration and expenses? Clarification is then needed regarding the extent to which leave of the court is required to apply trust assets in payment of a liquidator's remuneration and expenses in such circumstances.

Cases that have considered these issues include:

- *Re MF Global*;
- *Re North Food Catering Pty Ltd* [2014] NSWSC 77; and
- *Re MINMXT Holdings Pty Ltd (in Liquidation)* [2017] NSWSC 156.

(e) *The basis on which a liquidator's remuneration and expenses may be approved*

The statutory regime provided in the Corporations Act for approval of liquidator's remuneration and expenses may apply, however this is not settled law. If that regime is not intended to cover the field, guidance is needed as to how they may have their fees approved, without making an otherwise unnecessary application to court.

Cases that have considered these issues include:

- *Re AAA Financial Intelligence Ltd (in Liquidation)* [2014] NSWSC 1270;
- *Templeton v Australian Securities and Investments Commission* [2015] FCAFC 137; and
- *Sanderson as Liquidator of Sakr Nominees Pty Ltd (in Liquidation) v Sakr* [2017] NSWCA 39.

## V. Effect of replacement of Trustee

18. Most State Trustee Acts provide that all assets other than those which require registration are transferred as a matter of law to the new trustee upon their appointment.<sup>4</sup> In the Northern Territory and South Australia such vesting occurs upon registration of the appointment of the new trustee.<sup>5</sup> In Queensland, the new trustee has a positive duty to cause the registration to change and can execute the relevant paperwork to cause any change in the registration to occur.<sup>6</sup> In all States there is no automatic transfer of land, but rather a transfer must be separately registered. As indicated above, where the assets are not automatically transferred they are held on a resulting or constructive bare trust by the old trustee for the new trustee pending transfer.<sup>7</sup>

---

<sup>4</sup> *Trustee Act 1925 (ACT)* s 9; *Trustee Act 1925 (NSW)* s 9; *Trustee Act 1898 (Tas)* s 15; *Trustee Act 1958 (Vic)* s 45; *Trustees Act 1962 (WA)* s 10.

<sup>5</sup> *Trustee Act (NT)* s 57; *Trustee Act 1936 (SA)* s 76.

<sup>6</sup> *Trusts Act 1973 (Qld)* s 15.

<sup>7</sup> *Lewis v Nortex Pty Ltd* (2013) 211 FCR 483, 503-4 [77].

19. In South Australia, it has been held that a trustee's right of indemnity exists in relation to trust liabilities incurred up to the date the old trustee is notified of the new trustee's appointment.<sup>8</sup> The timing of the cut off for the indemnity may differ between States pursuant to the different legislative provisions referred to above.

## VI. Liquidator's duties

20. The courts have held that a liquidator dealing with trust assets has two primary duties, namely:

- a) To distinguish which assets of the company are owned by the company, and which are held beneficially for someone else; and
- b) To act reasonably to protect the trust assets.<sup>9</sup>

21. Justice Mandie of the Victorian Supreme Court has gone further and stated that in an appropriate case, and subject to the liquidator not being liable to incur expense in relation to the winding up unless there is sufficient funds available, the liquidator should:

- a) identify the trust's constituent documents;
- b) ascertain the nature and value of the trust assets and trust liabilities;
- c) investigate the financial relationship between the trustee and the trust;
- d) identify the trust's creditors and beneficiaries; and

---

<sup>8</sup> *Garra Water Investments Pty Ltd (in Liquidation) v Ourback Yard Nursery Pty Ltd* [2012] SASC 44 (26 March 2012) [39].

<sup>9</sup> *Porter v Miller Street Pty Ltd* [2008] FCAFC 77, (14 May 2008) [44] per Sundberg, Jacobson and Gordon JJ.

- e) consider any matters necessary to determine appropriate action to be taken in relation to the trust on behalf of the trustee, including action to preserve trust assets or to wind up the trust where appropriate and where there is express power to do so.<sup>10</sup>
22. Justice Ferguson of the Victorian Supreme Court (as she then was) has taken the duties referred to by Mandie J one step further where there is no automatic removal clause in a trust deed, by finding that the company should continue to exercise all of its powers as trustee of the company, including exercising its rights of indemnity and exonerations out of the trust property including its rights of sale of the trust assets if conferred by the trust instrument.<sup>11</sup>
23. As part of their duty in identifying the assets, liquidators must also review the validity of any security held over them and the validity of any appointment made under that security.
24. Where a company holds assets on trust, it has no beneficial interest in those assets (other than in support of its right to indemnity) as do the beneficiaries of the trust. The liquidation of the company does not alter this position.
25. Where a liquidator has doubt over which of the company's assets are held on trust, it is appropriate for the liquidator to seek directions.<sup>12</sup>

## **VII. Trustee's right of indemnity and recoupment**

26. It is trite that under trust law a trustee is the legal person who enters into transactions on behalf of a trust (which is not a separate legal entity) and that a trustee has a right of indemnity in relation to any

---

<sup>10</sup> *Irvine v Australian Sharetrading and Underwriting Ltd (in Liquidation)* (1996) 22 ACSR 765, 783.

<sup>11</sup> *Carrafa and Cauchi v Metroboore Australia Pty Ltd (in Liquidation)* [2014] VSC 247 (24 May 2014) [9].

<sup>12</sup> See *Bastion v Gideon Investments Pty Ltd (in Liquidation) (No 2)* (2000) 35 ACSR 466.

liability they so incur out of the trust assets. In *Octavo Investments Pty Ltd v Knight*<sup>13</sup> (**Octavo**) the High Court of Australia described a trustee's right of indemnity as follows:

If the trustee has incurred liabilities in the performance of the trust then he is entitled to be indemnified against those liabilities out of trust property and for that purpose he is entitled to retain possession of the property as against the beneficiaries. The trustee's interest in the trust property amounts to a proprietary interest and is sufficient to render the bald description of the property as 'trust property' inadequate. It is no longer property held solely in the interests of the beneficiaries of the trust...<sup>14</sup>

27. As illustrated by the above passage the right of indemnity creates a charge or lien which is proprietary in nature. This interest is beneficially owned by the trustee.
28. In *Custom Credit Co Ltd v Ravi Nominees Pty Ltd* (1992) 8 WAR 42, the Western Australian Court of Appeal summarised the position of a trustee as follows:
  - i. A trustee is personally liable for debts incurred as trustee in the administration of the trust fund: see *Vacuum Oil Co Pty Ltd v Wiltshire* (1945) 72 CLR 319, 335 (**Vacuum Oil**).
  - ii. A trustee has a right to reimburse itself out of trust property for all expenses reasonably and properly incurred in the execution of its powers and duties as trustee. Alternatively, the trustee can pay those expenses out of trust property: *Vacuum Oil* at 335-336.
  - iii. The right to reimbursement is commonly referred to as a right of recoupment, and the right to pay expenses out of trust is referred to as a right of exoneration. They are species of a wider entitlement called a right of indemnity.

---

<sup>13</sup> [1979] HCA 61.

<sup>14</sup> (1979) 144 CLR 360, 369-70. per Stephen, Mason, Aikin and Wilson JJ.

- iv. The right of indemnity arises at the time when the liability is incurred.
  - v. The charge or lien arises in equity by virtue of the trust relationship. The trustee has a charge or lien over trust property, to enable them to enforce the right of indemnity.
  - vi. The equitable charge or right of lien arises whether in the context of exoneration or recoupment.
  - vii. It is an incident of the equitable charge or lien which supports the right of indemnity that a trustee is entitled (as against beneficiaries) to retain possession of the trust property until the right of indemnity has been satisfied: *Stott v Milne* (1884) 25 Ch D 710, 715.
  - viii. A creditor of a trustee does not have direct access to trust assets to satisfy the liability and, even after a judgment, cannot levy execution against trust assets: *Savage v Union Bank of Australia Ltd* (1906) 3 CLR 1170 at 1186.
  - ix. However, a creditor of a trustee is entitled to be subrogated to the trustee's right of indemnity out of trust assets: *Re Evans; Evans v Evans* (1887) 34 Ch D 597.<sup>15</sup>
29. The above summary was adopted by the Victorian Supreme Court in *Gunns Finance Ltd*<sup>16</sup> and is similar to that put forward by Austin J in *Re Trim Perfect Australia Ltd*<sup>17</sup> and Coldroy J in *Prior v Simeon*.<sup>18</sup>
30. A trustee is entitled to be exonerated out of the trust assets for those liabilities that have been incurred but which have not been paid.<sup>19</sup>

---

<sup>15</sup> (1992) 8 WAR 42, 52-3.

<sup>16</sup> *Gunns Finance Ltd (in Liquidation) v WA Blue Gum Ltd* (2013) 281 FLR 121,148 [152].

<sup>17</sup> *Trim Perfect Australia Pty Ltd (in Liquidation) v Albrook Constructions Pty Ltd* [2006] NSWSC 153 (7 March 2006) [20] cited in *Australian Securities and Investments Commission v Letten (No 17)* (2011) 286 ALR 346, 350-1 [13].

<sup>18</sup> *Prior v Simeon* [No 2] [2011] WASC 61 (10 March 2011) [21].

<sup>19</sup> *Re Octavo Investments Pty Ltd v Knight* (1979) 124 CLR 360, 367; *Chief Commissioner of Stamps For New South Wales v Buckle* (1998) 192 CLR 226, 246.

The right of recoupment applies where the trustee has paid a trust liability from their own funds and seeks reimbursement. As indicated above, the right of indemnity is supported by an equitable lien over the trust assets held by the trustee.<sup>20</sup> The equitable lien takes priority over the interests of the beneficiaries. The right of indemnity is limited to liabilities incurred when acting as trustee.

31. A trustee's right of indemnity is however qualified as it does not apply to a liability arising out of a breach of trust, a breach of duty, or conduct which was criminal or fraudulent in nature.<sup>21</sup> The indemnity is also not available where the liability was unreasonable or unnecessary and therefore not properly incurred.<sup>22</sup> Not all breaches of trust will give rise to a loss of indemnity, although a breach of a core duty will.<sup>23</sup> The right of indemnity is also subject to a trustee making good any loss it has caused.<sup>24</sup>
32. A trustee has a right to seek indemnity out of a trust fund without judicial intervention where property of the trust is not required to be sold (ie: where funds are held in a bank account or cash on hand).<sup>25</sup>
33. Where the assets of a trust are insufficient to satisfy the trustee's right of indemnity the trustee may have a right of recoupment from the beneficiaries who are *sui juris* and have received trust property, in proportion to their respective equitable interests.<sup>26</sup> In practice, this right is usually only exercised after the trustee has exhausted the

---

<sup>20</sup> *TNT Building Trades Pty Ltd v Benelong Developments Pty Ltd (Administrator Appointed)* (2012) 91 ACSR 17, 27.

<sup>21</sup> *Gatsios Holdings Pty Ltd v Kritharas Holdings Pty Ltd (in Liquidation)* [2002] NSWCA 29; *Australian Securities and Investments Commission v Letten (No 17)* (2011) 286 ALR 346, 351 [14].

<sup>22</sup> *O'Keeffe v Hayes Knight GTO Pty Ltd*; (2005) 218 ALR 604, 606-7, [14] and *Nolan v Collie* (2003) 7 VR 287,306-8 [51]-[53].

<sup>23</sup> See *Nolan v Collie* (2003) 7 VR 287, 307-8 [51]-[53]; *Australian Securities and Investments Commission v Letten (No 17)* (2011) 286 ALR 346, 352 [15]-[17].

<sup>24</sup> *RWG Management Ltd v Commissioner for Corporate Affairs* [1985] VR 385, 397-8; *Warne v GDK Financial Solutions Pty Ltd*; *Billingham v Parbery* [2006] NSWSC 259, [192].

<sup>25</sup> *Prior v Simeon* [2010] WASC 382 (10 December 2010) [21]; *Re Winter Holdings (WA) Pty Ltd* [2015] WASC 162 (11 May 2015) [51].

<sup>26</sup> *Hardoon v Belilios* [1901] AC 118, 123-4; *Balkin v Peck* (1998) 20 ATR 15.

right to indemnity out of the trust estate.<sup>27</sup> This right is exercisable where beneficiaries had a distribution paid to them, or have otherwise received trust property where there are outstanding actual or contingent liabilities of the trust.

34. Professor Ford has opined that this right of recoupment does not extend to discretionary trusts as all beneficiaries may not be *sui juris* or have a present entitlement to the trust's assets.<sup>28</sup>
35. A right of recoupment will not exist where there is a specific and lawful provision to the contrary in the trust instrument.<sup>29</sup> In some States, including New South Wales and Queensland, a trustee cannot give up their rights of indemnity or recoupment.<sup>30</sup> It is however debatable as to whether a trustee can agree to give up the right of indemnity or recoupment.<sup>31</sup>

*(a) Liquidator's power of sale*

36. Section 197(1) of the Corporations Act to a limited extent recognises the existence of trusts by making directors personally liable to discharge a debt of the corporation where the corporation is acting or purporting to act as trustee but is not entitled to claim indemnity against that liability by reason of one or more of the circumstances set out in section 197(1)(b).
37. As indicated above, the trustee's proprietary interest is enforceable against other assets by a judicial sale or appointment of a receiver,

---

<sup>27</sup> *JW Broomhead (Vic) Pty Ltd (in Liquidation) v JW Broomhead Pty Ltd* [1985] VR 891, 936-7.

<sup>28</sup> Ford H A J "Trading Trusts and Creditors Rights" [1981] *Melbourne University Law Review* 1, 7-8.

<sup>29</sup> *Hardoon v Belilios* [1901] AC 118,127; *RWG Management Ltd v Commissioner for Corporate Affairs (Vic)* [1985] VR 385, 394; *McLean v Burns Philp Trustee Co Pty Ltd* (1985) 2 NSWLR 623; *Chief Commissioner of State Revenue v CCM Holdings Trust Pty Ltd* [2014] NSWCA 42 (7 March 2014) [72]; *Franknelly Nominees Pty Ltd v Abrugiato* [2013] WASCA 285 (6 December 2013) [220].

<sup>30</sup> See eg: *JA Pty Ltd v Jonco Holdings Pty Ltd* (2000) 33 ACSR 691, 713; *Kemtron Industries Pty Ltd v Commissioner of Stamp Duties (Qld)* [1984] 1 Qd R 576, 585.

<sup>31</sup> See *Franknelly Nominees Pty Ltd v Abrugiato* [2013] WASCA 285 (6 December 2013) [220]-[242].



and cannot be sold without curial intervention unless authorised by the trust deed.<sup>32</sup> This has however been questioned in *Apostolou* wherein Finkelstein J stated that the power of sale is conferred upon liquidators of trustee companies under section 477(2)(c) of the Corporations Act and as such it is not necessary to seek leave to sell assets.<sup>33</sup> Justice Finkelstein cited *UTSA Pty Ltd (in Liquidation) v Ultra Tune Australia Pty Ltd* as supporting his position as to the width of section 477.<sup>34</sup> A review of that later decision and the original decision appealed from reveals that UTSA Pty Ltd did not act as a trustee and that it was an application under section 511 of the Corporations Law seeking orders that they be authorised to enter into a deed pursuant to which the causes of action which had vested in the company in liquidation were assigned.<sup>35</sup> This decision was followed in *Kitay re South West Kitchens (WA) Pty Ltd* upon the basis that it was at the time the only decision of the Federal Court that expressly dealt with the matter.<sup>36</sup>

38. The position that the sale of trust assets is authorised by section 477 is not universally accepted and has been doubted by Brereton J of the New South Wales Supreme Court in *Re Stansfield DIY Wealth (in Liquidation)*<sup>37</sup> (**Re Stansfield**). His Honour stated that the power granted to a liquidator under section 477(2)(c) did not extend to the beneficial interest in the trust property as it was not “property of the company”.<sup>38</sup> His Honour then reverted to the traditional position and suggested that the appropriate course of action in that case was to

---

<sup>32</sup> *Trim Perfect Australia Pty Ltd (in Liquidation) v Albrook Constructions Pty Ltd* [2006] NSWSC 153 (7 March 2006) [20]; *Prior v Simeon* [2010] WASC 382 (14 December 2010) [21]; *Apostolou v VA Corporation of Aust Pty Ltd* [2011] FCAFC 103 (15 August 2011) [45]; *Re Stansfield DIY Wealth (in Liquidation)* [2014] NSWSC 1484 (30 October 2014).

<sup>33</sup> (2010) 77 ACSR 84.

<sup>34</sup> *Apostolou v VA Corporation (Aust) Pty Ltd* (2010) 77 ACSR 84, 94 citing *UTSA Pty Ltd (in Liquidation) v Ultra Tune Australia Pty Ltd* (1996) 21 ACSR 457.

<sup>35</sup> See *UTSA Pty Ltd (in Liquidation) v Ultra Tune Australia Pty Ltd* (1996) 21 ACSR 457; *UTSA Pty Ltd (in Liquidation) v Ultra Tune Australia Pty Ltd* [1997] 1 VR 667.

<sup>36</sup> [2014] FCA 670.

<sup>37</sup> [2014] NSWSC 1484 (30 October 2014); followed *SMP Consolidated Pty Ltd (in Liquidation) v Posmot Pty Ltd* [2014] FCA 1382 (9 December 2014).

<sup>38</sup> *Ibid* [30]; see also *Re Independent Contractor Services (Aust) Pty Ltd (No 2)* (2016) NSWSC 106, [2] (23 February 2016).

appoint the liquidator as the receiver of the trust property to facilitate the sale of the trust property. His Honour had previously expressed the view that the right of indemnity is enforced by either a judicial sale or the appointment of a receiver.<sup>39</sup> This view was consistent with a number of earlier decisions.<sup>40</sup>

39. The position expressed in *Re Stansfield* is fortified by a number of cases after *Apostolou*, in which liquidators have sought permission or power to sell assets.<sup>41</sup> Those decisions in part were based upon circumstances wherein the company had been removed as trustee but still held assets under bare trust. There are also a number of more recent decisions where the liquidators of trustee companies have sold the assets of a trust to satisfy the right of indemnity and subsequently upon releasing the trust assets sought directions under section 1318 of the Corporations Act and the relevant State Trustee Act to be excused for any breach of trust.<sup>42</sup> Such applications would have been unnecessary if a liquidator had power to sell the trust assets pursuant to section 477(2)(c).

40. The decision of the court as to whether to appoint a liquidator as receiver of the trust or to simply grant them power to sell the trust assets is often governed by the factual circumstances. In *Re Stansfield* the company acted as trustee of a superannuation fund and it was illegal for a company in liquidation to act in that capacity. The liquidator was therefore appointed as receiver. Similarly in *Winter Holdings*<sup>43</sup> the company as trustee was the holder of a liquor licence and wished to continue to trade pending sale in order to satisfy its

---

<sup>39</sup> *Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* (2008) 74 NSWLR 550, 560 [46].

<sup>40</sup> See eg: *Trim Perfect Australia Pty Ltd (in Liquidation) v Albrook Constructions Pty Ltd* [2006] NSWSC 153 (7 March 2006) [20].

<sup>41</sup> *Caterpillar Financial Australia Limited v Ovens Nominees Pty Ltd* [2011] FCA 677 (14 June 2011); *Garra Water Investments Pty Ltd (in Liquidation) v Ourback Yard Nursery Pty Ltd* [2012] SASC 11; *Re Neeeat Holding (in Liquidation)* [2013] FCA 61 (8 February 2013); see also *Re Winter Holdings (WA) Pty Ltd* [2015] WASC 162 (11 May 2015) [41] – [61].

<sup>42</sup> *Pleash v Suncoast Restoration Pty Ltd (in Liquidation)* (2013) 211 FCR 203; *Fletcher re Starrit Pty Ltd (in Liquidation)* [2012] FCA 803 (31 July 2012); *Theobald, in the matter of Finplas Pty Ltd* [2014] FCA 31.

<sup>43</sup> *Re Winter Holdings (WA) Pty Ltd* [2015] WASC 162 (11 May 2015).

right of indemnity. The liquidator was appointed as receiver of the trust.

*(b) Property of the Company*

41. As partially cited above, in *Octavo* the High Court found in relation to a claim under the previous version of section 122 of the *Bankruptcy Act 1966* (Cth) (**Bankruptcy Act**) that:

The trustee's interest in the trust property amounts to a proprietary interest, and is sufficient to render the bald description of the property as "trust property" inadequate. It is no longer property held solely in the interests of the beneficiaries of the trust and the trustee's interest in that property will pass to the trustee in bankruptcy for the benefit of the creditors of the trust trading operation should the trustee become bankrupt.<sup>44</sup>

42. It is arguable that this position has been recently brought into question by the Supreme Courts of New South Wales and Victoria who have held that the Liquidator's right of indemnity is not property of the company.<sup>45</sup>
43. As was highlighted in *Re Amerind*, if the Liquidator's right of indemnity is not the property of the company, then it is possible that the trust assets will not be the subject of any security granted by the company and a receiver appointed over the company will not be able to enforce against trust assets.

*(c) Application of claw back provisions*

44. If trust assets are to be treated separately from assets or property of the company and the Corporations Act does not apply to the

---

<sup>44</sup> *Octavo Investments Pty Ltd v Knights* (1979) 144 CLR 360, 370.

<sup>45</sup> See *Re Independent Contractor Services (Aust) Pty Limited (in Liquidation) (No 2)* [2016] NSWSC 106 (23 February 2016); *Woodgate re Bell Hire Services Pty Ltd (in Liquidation)* [2017] FCA 1583 (23 December 2016); *Re Amerind Pty Ltd (Receivers and Managers appointed) (in Liquidation)* [2017] VSC 127 (23 March 2017).

distribution of trust assets as is suggested,<sup>46</sup> the question arises whether the clawback provisions of Part 5.7B of the Corporations Act apply to transactions involving trust assets. This in part would depend on whether any transfer of property of the trust falls within the definition of a “transaction” as set out in section 9 of the Corporations Act. If trust assets are not property of the company then generally only payments by the company would fall within the definition of a transaction. This would limit the type of transactions that would be recoverable by a liquidator where the company acts as trustee, compared to a liquidator of a company which did not operate in a trustee capacity.

45. The above result appears to be inconsistent with what was said by the High Court in *Octavo* where it was found that a liquidator could rely upon the preference provisions contained in section 122 of the Bankruptcy Act to render void payments made by a company acting as trustee of the trading trust and that such money was repayable to the company.<sup>47</sup> The applicable legislation under which the company was wound up was the *Companies Act 1961-1975* (Queensland).

### **VIII. Liquidator’s remuneration and expenses**

46. The law in relation to the extent to which a liquidator’s remuneration and expenses are covered by the right of indemnity may differ between the States. In Victoria and South Australia where a company only acts as trustee of the trust, the trustee’s right of indemnity extends to include the liquidator’s costs and expenses.<sup>48</sup> In New South Wales the same rule would appear to apply, subject to a court

---

<sup>46</sup> See *Re Independent Contractor Services (Aust) Pty Limited (in Liquidation)(No 2)* [2016] NSWSC 106 (23 February 2016); *Re Amerind Pty Ltd (Receivers and Managers appointed) (in Liquidation)* [2017] VSC 127 (23 March 2017).

<sup>47</sup> *Octavo Investments Pty Ltd v Knights* (1979) 144 CLR 360.

<sup>48</sup> *Re Enhill Pty Ltd* [1983] VR 561, 572; *Re Suco Gold Pty Ltd (in Liquidation)* (1982) 33 SASR 99,110.

order being obtained approving both the right to claim such costs and expenses and the quantum (see also paragraph 49 below).<sup>49</sup>

47. Where a company is trustee of more than one trust it is appropriate to seek court directions as to the apportionment of costs and expenses of liquidation between the trusts.<sup>50</sup>
48. Where the company acts both on its own behalf and as trustee the costs can be apportioned such that the remuneration attributable to the statutory liquidation work would fall on the assets beneficially owned by the company whereas those costs which relate to administering the trust assets fall on the trust fund.<sup>51</sup> If the assets that are beneficially owned by the company are insufficient to pay for statutory work, the balance can be paid from the trust fund, subject to a court order.<sup>52</sup>
49. More recently Brereton J of the New South Wales Supreme Court found that the quantum of the liquidator's remuneration and expenses that are claimable may not be the same as that which has been approved as claimable against the company in accordance with the provisions of the Corporations Act, as either the beneficiaries or the court are required to approve them. Approval of the company's creditors does not suffice. A liquidator's remuneration and expenses claimable against the trust's assets must be reasonable and proportionate to the difficulty or importance of the task being performed.<sup>53</sup> The quantum of these fees can be approved based upon the percentage of any amount recovered.

---

<sup>49</sup> *Re North Food Catering Pty Ltd* [2014] NSWSC 77; *Re MF Global Limited (in Liquidation)* (No 2) [2012] NSWSC 1426 (23 November 2012); *Re MINMXT Holdings Pty Ltd (in Liquidation)* [2017] NSWSC 156 (28 February 2017) [14]-[15]; *Re AAA Financial Intelligence Ltd (in Liquidation)* [2014] NSWSC 1270 (17 September 2014).

<sup>50</sup> *Re Suco Gold Pty Ltd (in Liquidation)* (1982) 33 SASR 99,110; *Re MF Global Australia Ltd (in Liquidation)* (No 2) [2012] NSWSC 1426 (23 November 2012) [55].

<sup>51</sup> *Re MF Global Australia Ltd (in Liquidation)* (No 2) [2012] NSWSC 1426 (23 November 2012) [55]; *Re North Food Catering Pty Ltd* [2014] NSWSC 77 [9].

<sup>52</sup> *Re North Food Catering Pty Ltd* [2014] NSWSC 77 (10 February 2014) [17].

<sup>53</sup> *Re AAA Financial Intelligence Ltd (in Liquidation)* [2014] NSWSC 1270 (17 September 2014); *Garra Water Investments Pty Ltd (in Liquidation) v Ourback Yard Nursery Pty Ltd* [2012] SASC 11 (26 March 2012) [40]; *Re Independent Contractor Services (Aust) Pty Ltd (No 2)* (2016) NSWSC 106, [31] - [35] (23 February 2016).

50. The concept of proportionality was one factor which the Full Federal Court and New South Wales Court of Appeal have determined is a factor that must be considered by a court in approving insolvency practitioners' fees.<sup>54</sup>

## IX. New Trustee's right to trust assets

51. There appears to be a difference of opinion between the States as to a replacement trustee's right to demand the trust assets held by the old trustee who has an equitable charge over the same in support of a right of indemnity. In *Re Suco Gold* the Full Court of the South Australian Supreme Court held that the old trustee was entitled to retain possession of trust property for the purposes of protecting and enforcing its right of indemnity. This right is superior to that of the new trustee.<sup>55</sup>
52. However, in the Supreme Court of New South Wales Brereton J in *Lemery Holdings* sought to distinguish what was said in *Re Suco Gold* as obiter and found that a former trustee cannot bring an action for possession of the property as their equitable charge can only be enforced by judicial sale or the appointment of a receiver.<sup>56</sup> He further found that a trustee's right to possess the trust property is only as against the beneficiaries or a judgment creditor<sup>57</sup> and that:

it follows in principle that a former trustee does not have a right to retain, as against a new trustee, the trust assets as security for an accrued right of indemnity, though the former trustee is entitled to ensure the new trustee does not take steps which will destroy, diminish or jeopardise the

---

<sup>54</sup> *Templeton v Australian Securities and Investments Commission* [2015] FCAFC 137 (18 September 2015) [32]-[38]; *Sanderson as Liquidator of Sakr Nominees Pty Ltd (in Liquidation) v Sakr* [2017] NSWCA 39 (10 March 2017) [64].

<sup>55</sup> *Re Suco Gold Pty Ltd Pty Ltd (in Liquidation)* (1983) 33 SASR 99, 109-110 followed in *Prior v Simeon* [No 2] [2011] WASC 61 (10 March 2011) [20].

<sup>56</sup> *Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* (2008) 74 NSWLR 550, 560 [46].

<sup>57</sup> *Ibid* [47]-[49].

old trustee's right of security, which subsists in trust assets after their transfer to the new trustee.<sup>58</sup>

53. In *Neeeat Holding* Kenny J of the Federal Court disagreed with this statement and adopted what Finkelstein J stated in *Apostolou*:

I acknowledge that *Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* [2008] NSWSC 1344 ... holds that a retiring trustee cannot retain possession of trust property as against a new trustee. With respect, in my opinion there is no doubt that a retiring trustee can hold trust property to secure his right of reimbursement against both the beneficiaries and a new trustee.<sup>59</sup>

54. In *Apostolou*, Finkelstein J argued that trust property may not include property in respect of which the former trustee retains an equitable interest.<sup>60</sup> This suggestion has not been raised in any of the more recent decisions on this area, but it is suggested that it may answer the argument put in *Lemery Holdings*.

## **X. Which creditors are entitled to proceeds of indemnity?**

55. At present the law in this area would appear to differ between the States. In Victoria pursuant to the Full Court decision in *Re Enhill* all creditors are entitled to share in the proceeds from indemnity.<sup>61</sup> This decision has however been questioned in other States and by the Federal Court.<sup>62</sup>

56. In South Australia, Western Australia and New South Wales it is argued that there is a distinction between the right of recoupment and the right of exoneration. Where a trustee has already paid the liability

---

<sup>58</sup> Ibid [50].

<sup>59</sup> *Re Neeeat Holding (in Liquidation)* [2013] FCA 61 (8 February 2013) [21].

<sup>60</sup> *Apostolou v VA Corporation (Aust) Pty Ltd* (2010) 77 ACSR 84, 94 [49].

<sup>61</sup> *Re Enhill Pty Ltd* [1982] VR 561, 564; followed in *Ramsay v National Australia Bank Ltd* [1998] VR 59, 68.

<sup>62</sup> See *13 Coromandel Place Pty Ltd v CL Custodians Pty Ltd (in Liquidation)* (1998) 30 ASCR 377; *Collie v Merlaw Nominees Pty Ltd* (2001) 37 ACSR 361, 373-6.

of the trust from their own funds and is seeking reimbursement under the right of indemnity then the proceeds are available for all creditors. However where a trustee is exercising their right of exoneration in relation to unpaid debts of the trust, then those trust creditors have priority over unsecured creditors to money recovered.<sup>63</sup> This would appear to be based upon the creditors' rights to be subrogated to the trustee's right of indemnity.<sup>64</sup>

57. It is argued that this dichotomy is readily explainable as, all other things being equal, the funds used to pay the trust creditors would have otherwise been available to pay all creditors of the company and therefore should be available to all creditors once the company goes into liquidation.<sup>65</sup>
58. The basis of distribution of distribution to creditors may also differ between the States with a recent decision of Brereton J of the New South Wales Supreme Court finding that the statutory order of priorities set out in the Corporations Act should not apply when payments are to be made out of trust funds.<sup>66</sup> This decision has now been followed in the Federal Court of Australia and by the Supreme Court of Victoria.<sup>67</sup> These decisions have adopted a *pari passu* distribution to all creditors (including employees who may not be paid their full entitlement and the Commonwealth's priority under section 560 under the Corporations Act).

---

<sup>63</sup> *Re Suco Gold Pty Ltd Pty Ltd (in Liquidation)* (1983) 33 SASR 99,107,109; *Commissioner of Taxation v Bruton Holdings Pty Ltd (in Liquidation)* (2008) 173 FCR 472, 498 [79]; *Re MF Global Australia Ltd (in Liquidation) (No 2)* [2012] NSWSC 1426 (23 November 2012) [55].

<sup>64</sup> *Agusta Pty Ltd v Provident Capital* [2012] NSWCA 26 [70]-[75]; *Commissioner of Taxation v Fitzroy All Pty Ltd* [2013] WASC 427.

<sup>65</sup> See Ford H A J "Trading Trusts and Creditors Rights" [1981] *Melbourne University Law Review* 1, 19-24.

<sup>66</sup> *Re Independent Contractor Services (Aust) Pty Ltd (No 2)* (2016) NSWSC 106, [24] - [26] (23 February 2016). This decision is not consistent with the decision of Gordon J in *Caterpillar Financial Australia Ltd v Ovens Nominees Pty Ltd* [2011] FCA 677, [30], followed by Collier J in *Fletcher, in the matter of Starrit Pty Ltd (in Liquidation)* [2012] FCA 803,[24].

<sup>67</sup> *Woodgate re Bell Hire Services Pty Ltd (in Liquidation)* [2017] FCA 1583 (23 December 2016); *Re Amerind Pty Ltd (Receivers and Managers appointed) (in Liquidation)* [2017] VSC 127 (23 March 2017).



59. Option 7 set out in the Consultation Paper suggests that the law “could be amended to make it clear that the priorities under section 556 in the Corporations Act (order of priorities for unsecured creditors) apply when distributing the surplus from the realisation of the trust assets of a company which is a corporate trustee” and notes the current uncertainty at common law.
60. Self-evidently, the current divergent regimes which may be applied depending on whether the entity in liquidation was a corporate trustee has considerable implications including (but not limited) to whether section 556 applies, whether subrogation is available to FEG or any other person or entity who has facilitated or consented to early payment to an otherwise priority ranking creditor, and other questions live in the distribution of trust assets.
61. Given the high number of entities which are corporate trustees, this raises considerable questions not only in relation to FEG and other statutory schemes, but also broader concerns regarding the trust assets to be dealt with. The desirability of certainty and uniformity is great.
62. Option 8 set out in the Consultation Paper suggests that the priority of employee entitlements under sections 443 and 561 of the Corporations Act be clarified, and noting that the “general costs” which it is proposed employee entitlements be paid ahead of do not include “those associated with the realisation of the relevant assets” at footnote 59 in the Consultation Paper. It would be desirable for it to be clear that such entitlements are not intended to take priority over any lien the Liquidator would ordinarily hold.<sup>68</sup>

## **XI. Public policy**

63. In liquidating the assets of a company that has acted as a trustee there are competing public policy considerations between protecting

---

<sup>68</sup> *Re Universal Distributing Co Ltd (in Liquidation)* (1933) 48 CLR 171.

the interests of beneficiaries, while allowing for a cost effective and not overly administratively burdensome winding up of the company. These competing factors are set out above.

64. It is submitted that the clawback provisions should apply to trust assets as they do to the company's assets, as the same public policy considerations apply in determining whether or not the transfer of the assets is by the company or the trust.
65. The basic principles of equity dictate the protection of the interests of beneficiaries on whose behalf the trust property is held. In the case of smaller trusts the beneficiaries will most probably include the directors of the company and their relatives and, as such, they will most probably be aware of the company's obligations and its right of indemnity. However in larger trusts (eg: property trusts or managed investment schemes) the beneficiaries may not even know that the trustee company has been placed into liquidation or that there are amounts due to it under its right of indemnity.
66. It is submitted that equity would require, prior to any sale of trust property, the liquidator or receiver to give the beneficiaries the right to retain the trust property by adopting other means to satisfy the company's right of indemnity. This is especially the case where the assets hold either a sentimental or strategic value to the beneficiaries. It is submitted that part of the role of the court in determining whether to appoint a receiver or approve a judicial sale is to ensure that the beneficiaries are offered this right, rather than simply having the trust assets sold without their knowledge or approval. Further it is argued that the beneficiaries have the right to ensure that at least market value is achieved for the assets and, where there is more than one asset, to in some circumstances have some input into the order in which they are sold.
67. The issue also arises as to whether beneficiaries should be able to offer a compromise to the company, and if so, whether it should be

treated in the same way as the company compromising any other debt owed to it. Such compromise would allow the beneficiaries to keep some or all of the trust assets either themselves or by their transfer to a replacement trustee.

68. As highlighted above the court will also review the extent and amount of a liquidator's remuneration and expenses that are claimable against the trust assets, as it may not equate to the full amount of the liquidator's remuneration and expenses that are approved and claimable against the company, as a different test applies as to what is claimable against the trust assets. Given that in a large number of cases the only asset of the company is the right of indemnity, liquidators are conflicted in attempting to apportion their approved costs between those which are claimable against the trust assets and those which are not. The courts to date have provided the necessary check and balance to assist liquidators overcome this conflict.
69. If these public policy considerations can be achieved without court intervention it is submitted that would be advantageous to the conduct of an orderly winding up of a company. However, given the present state of our insolvency laws and the different types of trusts that exist which give rise to different competing interests, it is difficult to see how this could be achieved. Further, liquidators by reason of their training as accountants do not at present have the necessary detailed training in the law of equity to appreciate the extent of the fiduciary and other duties owed by the company and its officers to the beneficiaries, and the different rights of those beneficiaries in so far as they relate to different types of trusts.
70. There are differing views within the Law Council of Australia on this aspect. A contrary view is that the potential beneficiaries of an insolvent trading trust should have no greater rights than shareholders in an insolvent company and that a Liquidator's rights to sell property of the trading trust should be untrammelled. This is especially the case where the liquidator is an official liquidator and

thereby an officer of the court. Where complex issues of trust arise liquidators will appreciate that they need to obtain legal advice.

71. It is therefore submitted that in order for a proper balancing of the competing factors set out above to occur an independent arbitrator must be involved. The courts have traditionally performed this role and have the most experience and public recognition in this area. It is therefore suggested that the courts should continue to perform this function.

## **XII. Submission for reform**

72. In Australia trusts are widely used for trading activities. In order to give business and liquidators certainty it is submitted that there should be uniformity between the States as to how trust assets will be used when a trustee is placed into liquidation arising out of the trading activities of the trust, and in particular, further consideration should be given to the Commission's recommendations referred to at paragraph 12 above.
73. In relation to each of the issues identified above it is submitted that the appropriate legislation be passed either by way of uniform amendments to each State and Territory's Trustee Act or the referral of power to the Commonwealth such that legislation will be introduced to confirm the following:-

### *(a) Liquidator's duties*

This should be as specified above, and referred to by Ferguson J in *Carrafa and Cauchi v Metroboore Australia Pty Ltd (in Liquidation)*.<sup>69</sup>

---

<sup>69</sup> [2014] VSC 247 (24 May 2014) [9].

*(b) Property of the company, liquidator's right of indemnity and power of sale*

The definition of "property" in the Corporations Act should be amended to make it clear that property of the company extends to the trust assets.

For the reasons specified above it is submitted that there must be some check on a liquidator's power of sale. It is submitted that this can be achieved by a procedure pursuant to which a liquidator issues a prescribed notice to all beneficiaries (and where it is a discretionary trust, to all main beneficiaries and any beneficiary who received a distribution in the 5 years prior to liquidation or has an unpaid beneficial entitlement) advising them of the amount claimed by the company in liquidation under its right of indemnity, and advising that unless they either pay out the amount owed under the right of indemnity or provide a written objection within a specified period that the identified trust property will be sold. If an objection is received, then the Liquidator would be obliged to issue proceedings and join the objector(s) as defendants.

*(c) Liquidator's remuneration and expenses*

It is submitted that the liquidator's approved remuneration and expenses as approved in accordance with the Corporations Law (ie: by a committee of creditors, the creditors, or the court) should be claimable out of trust assets, with court approval and apportionment only being required where there are multiple trusts, or the company acted on its own behalf and as a trustee. The court should authorise Associate Justices or Masters to make these determinations.

*(d) New Trustee right to trust assets*

It is submitted that the decision of Brereton J in *Lemery Holdings* should not be followed, and this position be legislated.

*(e) Which creditors are entitled to the proceeds of the indemnity*

For public policy reasons it is submitted that trusts are easily identifiable now in modern commerce, as they have separate ABNs as well as the ability to register Personal Property Securities registrations over trust assets against the ABN of the trust rather than the ACN of the company. The position should now be that trust assets should first be applied in payment of trust debts including the trustee's right of indemnity and the liquidator's remuneration and expenses, and that such assets should only be available to pay the trustee's other debts pursuant to a court order. Further it is submitted that the statutory order of priorities applicable to the property of the company under the Corporations Act should apply to the distribution of the trust assets of an insolvent trading trust.

*(f) Claw back provisions*

It is submitted that the law should be clarified to ensure that the claw back provisions contained in the Corporations Act apply to transactions involving trust assets held by corporate trustees.

### **XIII. Recommendation**

74. A corporate trustee should be permitted to sell trust assets without court order, subject to obtaining the consent of the beneficiaries (or at the very least, being given notice of any proposed sale). If the beneficiaries wish to dispute the sale, then the issue should be determined by the court.
  
75. Subject to the above, the law should be clarified to ensure that a corporate trustee has power to sell assets of the company held on trust. This may be achieved by clarifying section 477 of the Corporations Act such that it confers power to sell trust assets.

76. These submissions and recommendations for reform are consistent with what was proposed by the Commission in Chapter 6 of the Harmer report in 1988.<sup>70</sup>
77. We recommend that the Commission be directed to again review the Harmer recommendations along with the further issues and recommendations covered in this submission.

## **PART B**

### **Remedies available to beneficiaries in dispute**

78. The use of corporate trustees of trading trusts raises complex issues.
79. While the trading trust vehicle may have tax advantages, difficulties arise when the company is insolvent, or when disputes arise.
80. The Corporations Act contains provisions dealing with these issues in the case of a company trading in its own right. But where the company trades in its capacity as a trustee of a trust the remedies under the Corporations Act and the States' Trustee Acts do not always provide a clear remedy.
81. The late Professor Harold Ford famously commented that "[t]he fruit of [the] union of the law of trusts and the law of limited liability companies is a commercial monstrosity."<sup>71</sup>
82. Justice Needham suggested in 1981 that "...the legislature should give consideration to the question whether trading trusts ... (no doubt entered into for taxation purposes) should be allowed to exist."<sup>72</sup>

---

<sup>70</sup> Australian Law Reform Commission 'General Insolvency Inquiry' [1988] ALRC 45

<sup>71</sup> HAJ Ford "Trading Trusts and Creditors' Rights" (1981) 13 MULR 1.

<sup>72</sup> *Re Byrne Australia Pty Ltd* (1981) 1 NSWLR 394, at 399.

83. This part of the submission is directed to the review of trading trusts in the context of oppression proceedings. The Victorian Law Reform Commission (**the Victorian Commission**) has published a report which recommends, amongst other things, amendments to the *Trustee Act 1958 (Vic)* (**Trustee Act**).<sup>73</sup>
84. The Victorian Commission considers that the law requires reform for reasons of clarity, simplicity and fairness. The review includes an analysis of a structure in which a business is operated by a company as trustee of a trust. It is the company that incurs liabilities, and it has a right of indemnity against trust assets. The wealth resides not in the company, but in the trust.
85. An oppressed shareholder can apply to the court under section 233 of the Corporations Act for a variety of orders, including an order for the compulsory purchase of shares. There is no similar remedy for a unit holder in a unit trust.
86. The result is that the parties, with the assistance of lawyers, are often compelled to resort to artificial, uncertain, frustrating and costly methods to resolve the dispute.
87. One option is to apply to the court for the appointment of a replacement trustee under section 48 of the Trustee Act. That course of action presupposes that there is a trustee willing and able to take on the role of trustee, and also that the business can continue unaffected by ongoing bickering between the beneficial owners.
88. One key recommendation of the Victorian Commission is that the Trustee Acts should be amended to include provisions similar to the provisions of section 233 of the Corporations Act.

---

<sup>73</sup> Victorian Law reform Commission, "Trading Trusts – Oppression Remedies" Report January 2015, [www.lawreform.vic.gov.au](http://www.lawreform.vic.gov.au).



89. In *Viglioroni v CPS Investment Holdings Pty Ltd*<sup>74</sup> the Victorian Supreme Court held that the court could order a buyout of units in a unit trust because section 53 of the Corporations Act defined “affairs of a body corporate” to include activities of the company acting as trustee.
90. By contrast, the New South Wales Supreme Court in *Trust Company Ltd v Noosa Venture 1 Pty Ltd*<sup>75</sup> insisted that no such order can be made because it relates to the trust and not to the company. The debate continues.
91. The Victorian Commission considers that traditional doctrines of trust have not kept pace with modern commercial reality, hence the need for review of trust law given the use of trusts in business ventures.
92. The recommendations of the Victorian Commission are sensible. They would add some certainty to what is presently an unsatisfactory state of affairs.
93. While any amendments of the kind proposed would apply only in Victoria, it is a start. Other jurisdictions can consider whether to follow the lead of the Victorian Commission.
94. In the meantime the report also serves as a useful reminder that lawyers and accountants recommending structures to their clients should consider whether trading trusts are suitable structures for business enterprises.

---

<sup>74</sup> (2009) 74 ACSR 282, a decision of Davies J.

<sup>75</sup> (2010) 80 ACSR 485, a decision of Windeyer AJ.

## **I Recommendation**

95. The Law Council of Australia endorses the proposed changes to the Trustee Act. The Council also encourages other jurisdictions in Australia to adopt similar amendments so that there can be uniformity of approach throughout Australia.
  
96. There is also a view that the amendments should apply to unit trusts only, not to discretionary trusts. That is on the basis that settlors of discretionary trusts and those involved in their establishment wanted the trustee to have absolute discretion, and the courts should not easily interfere with that discretion.