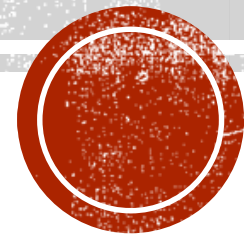


# LIQUIDATORS OF CORPORATE TRUSTEES

The Australian Perspective

David W Marks QC

Liability limited by a scheme approved under professional standards legislation



# INTRODUCTION TO TRUSTEE INSOLVENCY

- Structure:
  - I have to give an overly long introduction
  - Then I deal with 4 special issues we are seeing in Australia



# WHY CONSIDER AUSTRALIA'S MISSTEPS?

- To avoid making them
- To run arguments emerging
- To steer government toward any needed law reform
  
- *Octavo Investments* is cited & applied in New Zealand
- Australia is still working out where that 1979 case leads



# THE COMMERCIAL MONSTROSITY

- Prof Harold Ford (1981):

*The fruit of this union of the law of trusts and the law of limited liability companies is a commercial monstrosity. The scope for frustrating creditors is considerable.*



# AT THE HEART – RIGHT OF INDEMNITY

- Against whom/what?
  - Beneficiaries
  - Property
- 2 rights:
  - Right of exoneration
  - Right of recoupment
- Support:
  - Lien
  - Lien not lost if trustee ousted (eg on insolvency event)



# DEALING THE TRUSTEE OUT

- Can contract on basis that creditor restricted to trustee's right against fund
- Seen with the large trust companies
- Inflexible



# ON INSOLVENCY

- What's available to the liquidator?

*Property held by the insolvent on trust for beneficiaries is excluded from distribution to the creditors, expressly under bankruptcy legislation, and by undisputed analogy in the case of corporations. It is not property of the company.*  
:Cth v Byrnes (VSCA), [62]

- This includes trustee's right of indemnity
- Confers proprietary interest in the trust property, which:
  - passes to trustee in bankruptcy
  - available to company, under administration of liquidator – but what does that mean?



# THE RULE BOOK

- How does trustee in bankruptcy/liquidator, deal with right of indemnity?
- Is it restricted to paying trust liabilities?
- Coming back to this...





# PPSA

- Whether trustee's lien has to be registered
- Incredibly complex
- Contemplated as required, *obiter dicta* in *Cth v Byrnes*
- Prior academic opinion against requirement
- This is a whole topic in itself – not going to solve today!



# SUBROGATION

- To the trustee's right of indemnity (recoupment), & lien
- Right or remedy?
- Consequences of being a remedy:
- The Great Apple & Pear Case – *Lerinda v Laertes*



# WORKED EXAMPLE OF SUBROGATION

Assets & liabilities of trust	\$	Pari passu	Apple grower subrogated to trustee
Cash	\$1000		
Apple grower	(\$1000)	\$500	\$1000
Pear grower	(\$1000)	\$500	\$0
Total liabilities	(\$2000)		
Deficiency	(\$1000)	\$1000	\$1000

Thus growers seeking subrogation in *Lerinda v Laertes* were denied the **remedy** of subrogation to the trustee's right of indemnity (and supporting lien).

Numbers fictionalised, and made more extreme for illustration.  
Disclosure - I argued the trustee's case against subrogation.



# TRUSTEE REMOVED ON INSOLVENCY EVENT

- Many deeds provide for this
- Australian courts are enforcing this
- But no loss of indemnity *per se*.
- Does have to give up title on demand. No loss of “lien”.
- If no new trustee appointed – insolvent is treated as bare trustee,



# LIQUIDATORS MUST BE PAID

- Australia seems to have settled on the idea that, for administering trust assets, look to equity not Corporations legislation
- Leaves an unsatisfactory level of uncertainty



# CROWN PRIORITIES

- This is a general issue, not restricted to trusts
- But a couple of issues show the particular effects on trusts and estates



# 4 PARTICULAR ISSUES

- Excluding right of indemnity
- Which “Rule Book” governs use of the right of indemnity
- Liquidators’ remuneration
- Re-assertion of Crown priority



# 1. RESTRICTING RIGHT OF INDEMNITY

- Possible by deed - as against beneficiaries
- Whether possible by deed - as against property
  - *No* - *Kemtron (FC) (Qd)*; *JA P/L v Jonco (NSW)*
  - *Yes* - *Franknelly (CA)(WA)*; *RW Management (Vic)*
  - Answer - probably depends on the State trusts statute
  - Australian conflict noted in NZ: *Burgess v Monk (2017)*
- Choice of law rules - can you select more flexible State law?
  - Choose by deed: *Augustus v Permanent Trustee Co (Canberra) Ltd (1971) 124 CLR 245*.
  - Must be *bona fide* choice?: *Golden Acres Ltd v Queensland Estates Pty Ltd [1969] QdR 378*





# CONSEQUENCES OF EXCLUDING RIGHT

- Section 197 *Corporations Act* --- director liability
- Problematic sub (1)(b): Not entitled to be fully indemnified out of trust assets solely because of:
  - (i) *a breach of trust by the corporation;*
  - (ii) *the corporation's acting outside the scope of its powers as trustee;*
  - (iii) ***a term of the trust denying, or limiting, the corporation's right to be indemnified against the liability.***



# 2. WHICH RULE BOOK?

- Equity is equality?
- Statutory priorities applicable to corporate insolvency?
- This point is on the way to the HCA...



# IS THERE A DIFFERENCE – EXONERATION?

- FCR headnote to *Lane v DCT* (Derrington J):

*However, and notwithstanding that the right of exoneration is also property of the bankrupt, the exercise of the right by the trustee in bankruptcy can only result in trust funds being transferred directly to trust creditors in payment of their debts. It is not capable of being used to create proceeds for distribution in the usual manner.*

- ASCR headnote to *Cth v Byrnes* (VSCA):

*Once it is accepted that the right of indemnity by way of exoneration is property of the insolvent corporate trustee, the insolvency legislation and the statutory priorities regime must apply.*



# NUMERIC EXAMPLE - DIFFERENT RULE BOOKS

- Simplified!

Position	Trust	Pari passu	Trust - s.556
Assets	\$500		
Employee liabilities	(\$500)	\$417	\$500
General creditors	(\$100)	\$83	\$0
Deficiency	(\$100)		



# 3. HOW DOES THE LIQUIDATOR GET PAID?

- Even this is not a neatly settled formula!
- Not simply an application to court based on *Corporations Act*
- Can be based on the equitable principle of rewarding someone for bringing a fund into existence
- But - If also non-trust assets – some restriction on resort to the fund created by administering trust assets
- Where no right of exoneration – arguable no right to be paid from trust assets  
: *Lane v DCT, [187] (under appeal)*



# 4. RE-ASSERTION OF CROWN PRIORITY

- Notable trend that Crown priorities given up in the 1980s are being re-asserted by the backdoor:
- Non-trust contexts – eg *Linc Energy* (special leave being sought to HCA) – attempt by a State to subvert Commonwealth statutory priorities
- Contexts having special impact on trusts (though also impacting non-trustees):
  - Section 254 ITAA36
  - Sections 260-145 & 260-150 TAA53 – deceased estates
  - Garnishee notices have seen a resurgence – see *Can Barz*, and *Ultra Thoroughbred*



# AVOIDING THE MISTAKES

- Don't have a Federation
- State in legislation the extent to which indemnity may be excluded
- State in legislation whether the general insolvency priorities apply, or whether trusts are a special breed
- Make clear how the insolvency practitioner is to be paid
- Try to convince the Crown not to re-assert Crown priority ☺

