FEDERAL COURT OF AUSTRALIA

Jones (Liquidator) v Matrix Partners Pty Ltd, in the matter of Killarnee Civil & Concrete Contractors Pty Ltd (in liq) [2018] FCAFC 40

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| File number: |  |
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| Judges: | **ALLSOP CJ, SIOPIS AND FARRELL JJ** |
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| Date of judgment: | 21 March 2018 |
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| Catchwords: | **TRUSTS AND TRUSTEES** – trustee’s right of indemnity – nature of the right of exoneration – application of right of exoneration against trust assets in circumstances where corporate trustee is insolvent **CORPORATE INSOLVENCY** – company that carried on business as trustee of trading trust – trustee company now in liquidation – application of trustee’s right of exoneration against trust assets in circumstances where corporate trustee is insolvent – whether right of exoneration is property of the trustee company – whether proceeds of right of exoneration available only to pay trust creditors on insolvency**CORPORATE INSOLVENCY** – priorities regime to be applied to proceeds of realisation of trust assets through the right of exoneration and to proceeds of unfair preference claim – whether priorities regime established by ss 555, 556, 560 and 561 of the *Corporations Act 2001* (Cth) to be applied**CORPORATE INSOLVENCY** – trustee company disqualified from acting as trustee upon entering into liquidation – sale of trust assets by liquidator – whether proprietary character of the trustee’s right of exoneration meant the liquidator had power under s 447(2)(c) read with s 447(2)(m) of the *Corporations Act 2001* (Cth) to sell the trust assets  |
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| Legislation: | *Bankruptcy Act 1966* (Cth), ss 5, 116, 122*Corporations Act 2001* (Cth), ss 9, 433, 436A, 439C, 477, 499, 500, 501, 511, 555, 556, 560, 561*Fair Entitlements Guarantee Act 2012* (Cth), ss 29, 31*Companies Act 1893* (WA), ss 154, 155, 163 (repealed)*Companies Act 1961-1975* (Qld), s 293 (repealed)*Trustee Act 1898* (Tas), s 27*Trustee Act 1925* (ACT), s 59*Trustee Act 1925* (NSW), s 59*Trustee Act 1936* (SA), s 35*Trustee Act 1958* (Vic), s 36*Trustee Act 1980* (NT), s 26*Trustees Act 1962* (WA), ss 71, 89*Trusts Act 1973* (Qld), s 72Companies Act 1862 (UK)Law of Property Amendment Act 1859 (UK), s 31Preferential Payments in Bankruptcy Amendment Act 1897 (UK)Preferential Payments in Bankruptcy Bill 1888 (UK)Trustee Act 1893 (UK), s 24Trustee Act 1925 (UK), s 30Trustee Act 1956 (NZ), s 38  |
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| Cases cited: | *13 Coromandel Place Pty Ltd v C L Custodians Pty Ltd (in liq)* (1999) 30 ACSR 377*Agusta Pty Ltd v Provident Capital Ltd* [2012] NSWCA 26; 16 BPR 30, 397*Apostolou v VA Corp Aust Pty Ltd* [2010] FCA 64; 77 ACSR 84*Apostolou v Va Corp Aust Pty Ltd* [2011] FCAFC 103*Bofinger v Kingsway Group Limited* [2009] HCA 44; 239 CLR 269*Bruton Holdings Pty Ltd (in liq) v Commissioner of Taxation* [2009] HCA 32; 239 CLR 346*CGU Insurance Ltd v One.Tel Ltd (in liq)* [2010] HCA 26; 242 CLR 174*Chief Commissioner of Stamp Duties (NSW) v Buckle* [1998] HCA 4; 192 CLR 226*Chief Commissioner of Stamp Duties v Buckle* (1995) 38 NSWLR 574*Commonwealth v Byrnes and Hewitt in their capacity as joint and several receivers and managers of Amerind Pty Ltd (Receivers and Managers appointed) (in liquidation)* [2018] VSCA 41*Cook v Italiano Family Fruit Company Pty Ltd* [2010] FCA 1355; 190 FCR 474*CPT Custodian Pty Ltd v Commissioner of State Revenue (Vic)* [2005] HCA 53; 224 CLR 98*Dowse v Gorton* [1891] AC 190*Erven Warnink BV v J Townend & Sons (Hull) Ltd* [1979] AC 731*Esso Australia Resources Ltd v Commissioner of Taxation* [1999] HCA 67; 201 CLR 49*Ex parte Edmonds* (1862) 4 DeG F & J 488; 45 ER 1273*Ex parte Garland* (1804) 10 Ves Jun 110; 32 Er 786*In re Blundell* (1884) 40 Ch D 370*In re Blundell; Blundell v Blundell* (1889) 44 Ch D 1*In re Johnson* (1888) 15 Ch D 548*In re Morgan; Pillgrem v Pillgrem* (1881) 18 Ch D 93*In re Raybould* [1980] 1 Ch 199*In re Richardson* [1911] 2 KB 705*In re Suco Gold Pty Ltd (In Liq)* (1983) 33 SASR 99*Jennings v Mather* [1901] 1 KB 108*Jennings v Mather* [1902] 1 KB 1*Johnston v Salvage Association* (1887) 19 QBD 458*Jenyns v Public Curator (Queensland)* [1953] HCA 2; 90 CLR 113*Kemtron Industries Pty Ltd v Commissioner of Stamp Duties* [1984] 1 Qd R 576*Kite v Mooney, in the matter of Mooney’s Contractor’s Pty Ltd (No 2)* [2017] FCA 653; 121 ACSR 158*Lamb v Cotogno* [1987] HCA 47; 164 CLR 1*Lane (Trustee), in the matter of Lee (Bankrupt) v Deputy Commissioner of Taxation* [2017] FCA 953*Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* [2008] NSWSC 1344; 74 NSWLR 550*Lewis v Nortex Pty Ltd (in liq)* [2013] FCAFC 56; 211 FCR 483*Liverpool Mortgage Insurance Company’s Case* [1914] 2 Ch 617*Mason v Pomeroy* 24 NE 202 (1890)*Moorgate Tobacco Co Ltd v Philip Morris Ltd (No 2)* [1984] HCA 73; 156 CLR 414*Moragne v States Marine Lines Inc* 398 US 375 (1970)*NA Kratzmann Pty Ltd v Tucker (No 2)* [1968] HCA 44; 123 CLR 295*Nokes v Doncaster Amalgamated Collieries, Limited* [1940] AC 1014*Octavo Investments Pty Ltd v Knight* [1979] HCA 61; 144 CLR 360*R v L* [1991] HCA 48; 174 CLR 379*Re AAA Financial Intelligence Ltd (in liq)* [2014] NSWSC 1004*Re ADM Franchise Pty Ltd* (1983) 7 ACLR 987*Re Amerind Pty Ltd (recs and mgrs. apptd)(in liq)* [2017] 320 FLR 118; VSC 127*Re Byrne Australia Pty Ltd (No 2)* [1981] 2 NSWLR 364*Re Byrne Australia Pty Ltd* [1981] 1 NSWLR 394*Re Crest Realty Pty Ltd* *(in liq) (No 2)* [1977] 1 NSWLR 664*Re Dallhold Investments Pty Ltd* [1994] FCA 738; 53 FCR 339*Re Enhill Pty Ltd* [1983] 1 VR 561*Re Exhall Coal Co Ltd* (1866) 35 Beav 449; 55 ER 970*Re Fresjac Pty Ltd (in liq)* (1995) 65 SASR 334*Re GB Nathan and Co Pty Ltd (in liq)* (1991) 24 NSWLR 674*Re Independent Contractor Services (Aust) Pty Ltd (in liq) (No 2)* [2016] NSWSC 106; 305 FLR 222*Re Indopal Pty Ltd* (1987) 12 ACLR 54*Re McLernon* [1995] FCA 539; 58 FCR 391*Re MINMXT Holdings Pty Ltd (in liq)* [2017] NSWSC 156*Re Staff Benefits Pty Ltd* [1979] 1 NSWLR 207*Re Stansfield DIY Wealth Pty Limited (in liq)* [2014] NSWSC 1484; 291 FLR 17*Savage v Union Bank of Australia* [1906] HCA 37; 3 CLR 1170*Sjoquist v Rock Eisteddfod Productions Pty Ltd* (1996) 19 ACSR 339*South Pacific Manufacturing Co Ltd v New Zealand Security Consultants & Investigations Ltd* [1992] 2 NZLR 282*The Juliana* (1822) 2 Dods 504; 165 ER 1560*The Ruta* [2000] 1 Lloyd’s Rep 359*Universe Tankships Inc of Monrovia v International Transport Workers Federation* (*The Universe Sentinel*) [1983] 1 AC 366*Vacuum Oil Co Pty Ltd v Wiltshire* [1945] HCA 37; 72 CLR 319*Vadasz v Pioneer Concrete Sa Pty Ltd* [1995] HCA 14; 184 CLR 102*Van Beeck v Sabine Towing Co* 300 US 342 (1937)*Woodgate, in the matter of Bell Hire Services Pty Ltd (in liq)* [2016] FCA 1583*Worrall v Harford* (1802) 8 Ves Jun 4; 32 ER 250Atiyah PS, “Common Law and Statute Law” (1985) 48 *Modern Law Review* 1Australian Law Reform Commission, *General Insolvency Inquiry*, Report No 45 (1988)D’Angelo N, “Commercial Trusts in Practice: The Trust as a Surrogate Company”, paper presented at the Annual Commercial and Corporate Law Conference convened in November 2016 by the Supreme Court of New South Wales Finn P, “Statutes and the Common Law” (1992) 22 *UWA LR* 7Finn P, “Statutes and the Common Law” in Corcoran S and Bottomley S (eds), *Interpreting Statutes* (Federation Press, 2005)Fratcher WF, *Scott on Trusts* (4th ed, Little Brown, 1987)Goode R, *Principles of Corporate Insolvency Law* (4th ed, Sweet & Maxwell, 2011)Gummow WMC, *Change and Continuity: Statute, Equity and Federalism* (Oxford University Press, 1999)Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths, 2016) Leeming MJ, “Equity: Ageless in the ‘Age of Statutes’” (2015) 9 *Jo of Equity* 108McPherson BH, “The Insolvent Trading Trust” in Finn PD (ed), *Essays in Equity* (Lawbook Co, 1985)Meagher RP and Gummow WMC, *Jacobs’ Law of Trusts in Australia* (5th ed, Butterworths, 1986)Pound R, “Common Law and Legislation” (1908) 21 *Harv LR* 383Story J, *Commentaries on Equity Pleading* (7th ed, Little Brown, 1865)Symes CF, *Statutory Priorities in Corporate Insolvency Law* (Ashgate Publishing Limited, 2008)Tetley W, *International Maritime and Admiralty Law* (Edition Yvon Blais, 2002)Thomas DR, *Maritime Liens* (Stevens, 1980)  |
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| Date of hearing: | 10-11 August 2017 |
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| Registry: | Western Australia |
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| Division: | General Division |
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| National Practice Area: |  |
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| Sub-area: | Corporations and Corporate Insolvency |
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| Category: | Catchwords |
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ORDERS

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|  | WAD 181 of 2016 |
| IN THE MATTER OF KILLARNEE CIVIL & CONCRETE CONTRACTORS PTY LTD ACN 085 230 486 (IN LIQUIDATION) |
| BETWEEN: | MARTIN BRUCE JONES IN HIS CAPACITY AS THE LIQUIDATOR OF KILLARNEE CIVIL & CONCRETE CONTRACTORS PTY LTD ACN 085 230 486 (IN LIQUIDATION)Plaintiff |
| AND: | MATRIX PARTNERS PTY LTD Defendant |
|  | COMMONWEALTH OF AUSTRALIAFirst Interested Person |
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|  | WESTPAC BANKING CORPORATIONSecond Interested Person  |

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| JUDGE: | ALLSOP CJ, SIOPIS AND FARRELL JJ |
| DATE OF ORDER: | 21 MARCH 2018 |

THE COURT ORDERS THAT:

1. The separate questions set down for hearing by the Full Court annexed to the orders of Siopis J made on 12 May 2017, as varied by the orders of Allsop CJ made on 21 June 2017, be answered as follows:

**Question 1:**

Are the assets of the Thompson Family Trust (**Trust**) as at the time of the resolution to wind up the Company (including the proceeds of sale of those assets) (**Trust Assets**) assets in the winding up of Killarnee Civil & Concrete Contractors Pty Ltd (In Liquidation) ACN 085 230 586 (**Company**) so that the liquidator had the power under section 477 of the *Corporations Act 2001* (Cth) to sell the Trust Assets?

**Answer 1:**

Each member of the Court answers “no”.

**Question 2:**

Are either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds to be applied by the Plaintiff in accordance with the priority regime established by sections 555, 556, 560 and 561 of the *Corporations Act*?

**Answer 2:**

As to the unfair preference proceeds, each member of the Court answers “yes”, with the qualification set out in [93]-[94] of the reasons of the Chief Justice, agreed in by Justice Siopis at [149] and by Justice Farrell at [199].

As to the realisation of the Trust Assets, the Chief Justice and Justice Farrell answer “yes”, but for the different reasons set out in their reasons for judgment; and Justice Siopis answers “no”.

**Question 3:**

Should the Plaintiff be directed under s 511 of the *Corporations Act* to deal with either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds as assets in the winding up of the Company?

**Answer 3:**

The Chief Justice answers the question “yes as to both”; Justice Siopis answers the question “yes” as to unfair preference proceeds, but “no” as to the realisation of trust assets; and Justice Farrell answers to the effect that directions should be given in accordance with the answer to question 2, which is in substance the same answer as the Chief Justice.

**Question 4:**

Alternatively, should the Plaintiff be directed under s 511 of the *Corporations Act* that either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds be distributed by the Plaintiff to unsecured creditors of the Trust pari passu after providing for the costs of administration (including the Administrators’ and Liquidators’ remuneration and expenses) only?

**Answer 4:**

Each member of the Court answers “no”, but the Chief Justice and Justice Farrell reach that answer for reasons different to those of Justice Siopis.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

REASONS FOR JUDGMENT

ALLSOP CJ:

## Introduction

1. Before the Court is an application for directions and declarations under s 511 of the *Corporations Act 2001* (Cth) and s 89 of the *Trustees Act 1962* (WA) by the liquidator of Killarnee Civil & Concrete Contractors Pty Ltd (**the Company**), Mr Martin Jones. The substantive issue in deciding the application is the proper legal approach to take to the proceeds of the exercise of the right of exoneration by a liquidator of a company that was the trustee of a trading trust.
2. The questions at the centre of the application are as follows: In circumstances of corporate insolvency how must the liquidator of a company, which was the trustee of a trading trust, treat the exercise and proceeds of the right of exoneration from assets of the trust? Does the right or do the proceeds form part of the general assets of the company that are available for the payment of all debts of the company, including costs and fees of the liquidator according to the regime of the *Corporations Act*? If not, must the right and the proceeds be used only for trust creditors? If so, and notwithstanding that conclusion, does the regime of the *Corporations Act* nevertheless apply to the distribution amongst trust creditors?
3. The issue has been the subject of discussion and of conflicting authorities for almost 40 years since the High Court’s decision in *Octavo Investments Pty Ltd v Knight* [1979] HCA 61; 144 CLR 360. For purposes of introduction it is sufficient to say that there appear to have been three approaches taken in the authorities: the first exemplified by the decisions of Needham J in *Re Byrne Australia Pty Ltd* [1981] 1 NSWLR 394 and in *Re Byrne Australia Pty Ltd (No 2)* [1981] 2 NSWLR 364; the second exemplified by the decision of the Full Court of the Supreme Court of Victoria in *Re Enhill Pty Ltd* [1983] 1 VR 561; and the third exemplified by the decision of the Full Court of the Supreme Court of South Australia in *In re Suco Gold Pty Ltd (In Liq)* (1983) 33 SASR 99. There is no decision of the Full Court of this Court on the subject. Because of the lack of agreement amongst courts of different jurisdictions on the question, it was thought appropriate to hear the matter in the original jurisdiction of the Court sitting as the Full Court.
4. After completion of these reasons and shortly prior to delivering judgment a five member bench of the Victorian Court of Appeal handed down judgment in *Commonwealth v Byrnes and Hewitt in their capacity as joint and several receivers and managers of Amerind Pty Ltd (Receivers and Managers appointed) (in liquidation)* [2018] VSCA 41. Their conclusions and reasons accord with much of what follows in answer to question 2. Their Honours did not decide whether *Re Enhill* or *In re Suco Gold* was correct. They decided, however, that the right of exoneration and the proceeds of its exercise were property of the company and were to be dealt with in accordance with the regime of the *Corporations Act* (there being no external creditors other than trust creditors of one business carried on under one trust). I have expressed the view in answer to question 2 that *In re Suco Gold* is correct. In maintaining that view after reading the Court of Appeal’s reasons in *Re Amerind*,I recognise the competing arguments and considerations so clearly articulated by the Court especially at [283] and [284]. In my view, there is no reason for the advent of liquidation to change the character and nature of the right (of exoneration) and the proceeds of its exercise. The inhering nature of the right is derived from its equitable source and can be, and should be, maintained under the regime of the *Corporations Act*, albeit with any necessary qualifications brought about by the terms of the Act in respect of payment of costs associated with the operation of the statutory insolvency regime and the operation of such provisions under the influence of cognate equitable principle.
5. Four separate questions were prepared in consultation with the liquidator and various representative creditors. I will set out those questions after briefly outlining the essential facts.
6. May I say at the outset that the parties and representatives have the Court’s gratitude for the assistance provided by all counsel.

## The essential facts

1. The Company was incorporated in 1998 and until its creditors resolved to wind it up under s 439C(c) of the *Corporations Act* on 9 December 2014 it carried on business in the concrete and civil construction business. Until 1 September 2014, the Company carried on that business under the direction of a board of directors. On that date, Mr Jones and others were appointed joint administrators of the Company under s 436A of the *Corporations Act.*
2. At all relevant times, before and after the appointment of the administrators, the Company carried on the business as trustee of one trust, the Thompson Family Trust (**the Trust**), created by deed dated 18 November 1998. The Company had a notional paid up capital of $2. It did not conduct business on its own account. It did not conduct business on behalf of any other trust. All its assets were held on the terms of the Trust. All claims and liabilities were entered into or incurred in furtherance of the objects and purposes of the Trust. There was no suggestion that any claim or liability had been entered into or incurred other than in the proper discharge of the functions and duties of the Company as trustee of the Trust.
3. Clauses 7.27 and 7.28 of the trust deed provided for powers to deal with the trust assets as follows:

9.27 to deal with, manage, transpose and realise any investments and all property constituting the Trust Fund or any property comprised in any security as the Trustee thinks fit in all respects as if the Trustee was the absolute and beneficial owner of the Trust Fund AND the Trustee shall not be accountable in any way whatsoever for any loss arising out of the making of any investment or out of the failure to realise any investment or out of the management of any investment;

9.28 to sell or otherwise dispose of any real or personal property or a share of interest therein of the Trust Fund and to join with any co-owner or co-owners or partner or partners in selling or otherwise disposing of the real or personal property by public auction, tender or private treaty at such price or prices and whether for cash or on terms and generally upon such terms and conditions as the Trustee thinks fit;

1. Clause 16 of the trust deed provided for an indemnity to the trustee in the following terms:

The Trustee shall be entitled to be indemnified out of the assets for the time being comprising the Trust Fund against liabilities incurred by the Trustee in the execution or attempted execution or as a consequence of the failure to exercise any of the trusts authorities powers and discretions hereof or by virtue of being the Trustee hereof but the Trustee shall not be entitled to be indemnified by any beneficiary personally in respect of any liabilities or other matters aforesaid other than in respect of any duty or tax which the Trustee is entitled to recover from the beneficiary by law.

1. Section 71 of the *Trustees Act 1962* (WA) is in the following terms:

A trustee may reimburse himself for or pay or discharge out of the trust property all expenses reasonably incurred in or about the execution of the trusts or powers.

1. After 1 September 2014, the administrators arranged for the Company to realise certain of the assets held as the trustee of the Trust including the collection of debts, and the sale of its business, plant and equipment.
2. The receipts of the administrators of the Company totalled some $9.5 million which was applied, in part:
	1. to meet the administrators’ remuneration and expenses in continuing to carry on the Company’s business and then in effecting the sale of the Company’s business, plant and equipment;
	2. to meet the administrators’ remuneration and expenses in relation to the administration of the Company; and
	3. to pay $500,000 to Westpac Banking Corporation (**Westpac**) which was a secured creditor of the Company. Westpac’s securities included a fixed and floating charge from the Company in its own right, and as trustee for the Trust.
3. On 9 December 2014, the creditors of the Company resolved to wind the Company up in accordance with s 439C(c); and in accordance with s 499(2A)(b) of the *Corporations Act*, Mr Jones, among others, thereupon became the Company’s liquidator for the purposes of the winding-up of the Company.
4. Clause 21 of the trust deed provided that the trustee would be disqualified from holding office if the trustee was a Company and entered into liquidation, whether compulsory or voluntary, other than a voluntary liquidation for the purposes of an amalgamation or reconstruction. The Company thereby ceased to hold office as trustee.
5. As liquidator of the Company (together with the other joint liquidators while they remained in office) Mr Jones received the balance of the money realised by the administrators, being a sum of $2,531,549, and otherwise caused the Company to realise the remaining assets of the Trust including:
	1. debtors ($1,972,137);
	2. real estate ($819,500);
	3. plant and equipment ($165,109); and
	4. miscellaneous refunds and interest ($340,166).
6. Mr Jones also recovered from the Australian Taxation Office, an amount of $4.5 million, as an unfair preference.
7. At no time prior to the realisation of any of the assets by the liquidators did anyone seek to appoint a new trustee; nor did any person make application for the appointment of a receiver, or receiver and manager in relation to the Trust or an application for a judicial sale of the trust assets.
8. In June and July 2016, deeds of variation purporting to replace the trustee, guardian and appointor under the trust deed were executed.
9. As liquidator of the company, Mr Jones holds some $4,129,317 representing the balance of all the receipts of the administrators and liquidators including the unfair preference proceeds after various payments, including:

(a) the liquidators’ remuneration and expenses ($766,230); and

(b) payments made to persons including former employees in relation to priorities afforded by ss 556 and 560 of the *Corporations Act.*

1. The debts and claims in the Company’s winding up comprised the following:

(a) $197,576.48 plus GST for the liquidators’ remuneration and expenses as at 30 April 2017;

(b) $2,005,000 as to priority unsecured debts or claims in relation to employee entitlements within s 556(1)(e)-(h) of the *Corporations Act*, including amounts to which the Commonwealth of Australia is subrogated as mentioned below; and

(c) $19,490,733.83 as to ordinary unsecured debts or claims and the debt owed to Westpac as described below.

1. Three parties have been named in the Further Re-Amended Interlocutory process: an ordinary unsecured creditor, Matrix Partners Pty Limited (as a defendant); the Commonwealth of Australia represented by the Department of Employment as a priority unsecured creditor in the winding-up of the Company in the amount of $148,039.81 due to advances made by it pursuant to the *Fair Entitlements Guarantee Act 2012* (Cth) and by virtue of s 560 of the *Corporations Act* and ss 29 and 31 of the *Fair Entitlements Guarantee Act* (as the first interested party); and Westpac as the holder of security with a debt owing of over $1.5 million (as the second interested party).
2. In the course of administration and winding-up of the Company, employee entitlements have been paid out of funds that were subject to the charge in favour of Westpac.
3. The following revised separate questions were set down for hearing:
4. Are the assets of the Thompson Family Trust (**Trust)** as at the time of the resolution to wind up the Company(including the proceeds of sale of those assets) (**Trust Assets**) assets in the winding up of Killarnee Civil & Concrete Contractors Pty Ltd (In Liquidation) ACN 085 230 586 (**Company**) so that the liquidator had the power under section 477 of the *Corporations Act* to sell the Trust Assets?
5. Are either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds to be applied by the Plaintiff in accordance with the priority regime established by sections 555, 556, 560 and 561 of the *Corporations Act*?
6. Should the Plaintiff be directed under s 511 of the *Corporations* Act to deal with either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds as assets in the winding up of the Company?
7. Alternatively, should the Plaintiff be directed under s 511 of the *Corporations Act* that either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds be distributed by the Plaintiff to unsecured creditors of the Trust pari passuafter providing for the costs of administration (including the Administrators’ and Liquidators’ remuneration and expenses) only?

## Further introductory remarks

1. The statutory context is that a company which traded as a trustee is being wound up under Ch 5 of the *Corporations Act.* Section 556 gives employees priority in the distribution of assets in the winding-up. Does it apply? The very same question would arise were there to be a floating charge (now called a circulating security interest) in circumstances where ss 433 and 561 require a receiver and a liquidator, respectively, to pay employees out of assets subject to the charge.
2. Affirmative answers would be given to these questions by following *Re Enhill* and *In re Suco Gold*, but for importantly different reasons. Recent first instance decisions have not done so and have expressed the view that the right of exoneration and proceeds thereof are not “property of the company” for the purposes of the *Corporations Act*, being property held on trust outside the operation of the *Corporations Act*: see generally *Re Independent Contractor Services (Aust) Pty Ltd (in liq) (No 2)* [2016] NSWSC 106; 305 FLR 222; *Woodgate, in the matter of Bell Hire Services Pty Ltd* [2016] FCA 1583; *Re Amerind Pty Ltd (recs and mgrs apptd) (in liq)* [2017] VSC 127; *Kite v Mooney, in the matter of Mooney’s Contractors Pty Ltd (No 2)* [2017] FCA 653; 121 ACSR 158; *Re MINMXT Holdings Pty Ltd (in liq)* [2017] NSWSC 156; and *Lane (Trustee), in the matter of Lee (Bankrupt) v Deputy Commissioner of Taxation* [2017] FCA 953.
3. There have been two particular points of controversy over the years as to the operation of trading trusts and relevant statutes, here the focus of priority provisions of the *Corporations Act.* The first is whether the (insolvent) trustee’s right of exoneration from trust assets (as distinct from its right of recoupment from trust assets) was property of the company available to satisfy debts of all creditors of the company, irrespective of whether they were so-called trust creditors of the trust against which the right was executed. That debate is focused on whether *Re Enhill* is to be followed in the view that the right of exoneration (as with the right of recoupment) is purely personal to the company and unattended by equitable obligation to pay the trust creditors. The second is whether, if *Re Enhill* is wrong, and the right of exoneration could only be used to pay liabilities of the Company undertaken in the carrying out of the trust in question, whether *In re Suco Gold* was correct that, nevertheless, the statutory order of priorities in the *Corporations Act* applied, or whether *Re Byrne* (and the later more recent cases) is (and are) correct that it did not apply and all trust creditors rank pari passu outside the operation of the *Corporations Act.*
4. The critical question for this application is the second question because if the statutory order applies, employees of the Company will receive priority; if it does not apply and a pari passu distribution occurs unaffected by the statute, they will not.
5. The submissions for the parties were to the effect (correctly) that the Court only had to decide the relevant questions recognising that all assets and liabilities were trust liabilities of one trust and did not have to deal with the problem of an insolvent corporate trustee having carried on business or activities on its own account as well as a trustee, or having carried on business as a trustee of more than one trust. Whilst it is only necessary to answer the questions in the form posed, the reasoning used to reach the answers must recognise the wider and different circumstances that may arise in other insolvencies.

## Summary of conclusions

1. In my respectful view, *Re Enhill* is wrong in its view as to the availability of the proceeds of the right of exoneration generally to all creditors and should not be followed in that regard, and *In re Suco Gold* should be followed as to the question of the application of the *Corporations Act* and in particular the order of priorities amongst the creditors entitled to participate in the proceeds of any right of exoneration.

## Applicable general principles

1. Subject to statute, a trust has no legal personality, being an equitable institution comprised of rights, duties and obligations, personal and proprietary, constituting (in private trusts) the relationship between beneficiaries, trustee and property. The institution involves the equitable obligation binding on the trustee to deal with the trust property for the benefit of the beneficiaries and for the purposes of the trust.
2. A corporation, as a legal person, may act as a trustee. Subject to the operation of general law and statute as to the duties and responsibilities of directors, the principles of equity and trusts attending trustees apply equally to corporations and natural persons acting as trustees.
3. Clause 21 of the trust deed had the effect that from 9 December 2014 the Company ceased to hold office as trustee. After that time, the liquidator took control of the property. His position is discussed below. His dealing with the property was not as trustee, except to the extent that the Company or he could be seen as a trustee de son tort, or in his own right as liquidator vindicating the Company’s right of exoneration. To the extent that the position of the liquidator or the Company can be equated with that of a bare trustee (see *Lewis v Nortex Pty Ltd (in liq)* [2013] FCAFC 56; 211 FCR 483 at 503-504 [77]), he or it had an obligation to protect trust assets: *CGU Insurance* *Ltd v One.Tel Ltd (in liq)* [2010] HCA 26; 242 CLR 174 at 182-183 [36].
4. Subject to any provision of a contract, the trustee is personally liable for debts or liabilities incurred in execution of its duties and powers in the business or affairs of the trust: *Re Johnson* (1880) 15 Ch D 548 at 552; *Vacuum Oil Co Pty Ltd v Wiltshire* [1945] HCA 37; 72 CLR 319 at 324 and 335; and *Octavo Investments* 144 CLR at 367. That liability arises in accordance with ordinary principles of law, whether statute, contract, tort, equity or restitution. At least in Anglo-Australian law, there is no direct access by the creditors to the assets of the trust, but in equity the creditors may be subrogated to the rights of the trustee against the trust assets: *Vacuum Oil* 72 CLR at 335.
5. Subject to the terms of the trust, the trustee is entitled to be indemnified against debts and liabilities incurred in the proper execution of its duties and powers under the trust out of the assets of the trust. Subject to the terms of the trust, such right of indemnity has priority over the claims of the beneficiaries, and is secured by a lien. Such indemnity may arise for satisfaction before or after the trustee has paid the debt or liability in question. If the trustee has used its own funds to pay the debt or meet the liability, the entitlement of access to the trust assets is a personal asset of the trustee, unattended by equitable obligation arising from the trust. If the trustee has not paid the debt, it has a right of exoneration from the trust assets; that is a right to use the trust assets to exonerate itself from liability for the debt or liability that has been incurred in carrying out the duties or functions of trustee. In either case, the trustee has a lien over the trust assets for the right of indemnity. The right of indemnity is a beneficial interest in the trust property that will be preferred to any beneficial interest of the cestuis que trust in the trust assets.
6. The following description of the right, found in Fratcher WF, *Scott on Trusts* (4th ed, Little Brown, 1987) Vol IIIA § 246, was approved by the High Court in *Chief Commissioner of Stamp Duties (NSW) v Buckle* [1998] HCA 4; 192 CLR 226 at 245 [47]:

Where the trustee acting within his powers makes a contract with a third person in the course of the administration of the trust, although the trustee is ordinarily personally liable to the third person on the contract, he is entitled to indemnity out of the trust estate. If he has discharged the liability out of his individual property, he is entitled to reimbursement; if he has not discharged it, he is entitled to apply the trust property **in discharging it**, that is, he is entitled to exoneration.

(emphasis added)

The expression of the entitlement to apply the trust property was directed to the discharging of the liability incurred by the trustee for the trust.

1. The sources of the right of indemnity are threefold: equitable principle, the terms of the trust (here cl 16 of the trust deed), and statute (here s 71 of the *Trustees Act*).
2. As to equitable principle, Lord Eldon said in *Worrall v Harford* (1802) 8 Ves Jun 4 at 8; 32 ER 250 at 252 (cited in *Buckle* 192 CLR at 245 [45]) that it was:

in the nature of the office of trustee … that the trust property shall reimburse him all the charges and expenses incurred in the execution of the trust.

1. Thus, in equitable principle, the right and its characteristics arise from its place in the trust relationship.
2. As to statute, trustee legislation in all States and Territories provides for reimbursement, recoupment and exoneration: *Trustee Act 1925* (ACT), s 59(4); *Trustee Act 1925* (NSW),
s 59(4); *Trustee Act 1980* (NT), s 26; *Trusts Act 1973* (Qld), s 72; *Trustee Act 1936* (SA),
s 35(2); *Trustee Act 1898* (Tas), s 27(2); *Trustee Act 1958* (Vic), s 36(2); *Trustees Act 1962* (WA), s 71 (set out above); also the *Trustee Act 1956* (NZ),s 38(2), all of which are derived from the *Law of Property Amendment Act 1859* (UK), s 31(2), the *Trustee Act 1893* (UK), s 24, and the *Trustee Act 1925* (UK), s 30(2).
3. In *Re Exhall Coal Co Ltd* (1866) 35 Beav 449 at 452-453; 55 ER 970 at 971, Lord Romilly MR said that the right of indemnity was a first charge on the trust property. In *Vacuum Oil* 72 CLR at 335, Dixon J described it as “a lien over the assets which takes priority over the rights in or in reference to the assets of the beneficiaries.” In *Octavo Investments* 144 CLR at 367, Stephen, Mason, Aickin and Wilson JJ described it as a “charge or right of lien”, saying:

The charge is not capable of differential application to certain only of such assets. It applies to the whole range of trust assets in the trustee’s possession except for those assets, if any, which under the terms of the trust deed the trustee is not authorised to use for the purposes of carrying on the business: *Douse v Gorton*.

…[T]here are then two classes of persons having a beneficial interest in the trust assets: first, the cestuis que trust, those for whose benefit the business was being carried on; and secondly, the trustee in respect of his right to be indemnified out of the trust assets against personal liabilities incurred in the performance of the trust. The latter interest will be preferred to the former, so that the cestuis que trust are not entitled to call for a distribution of trust assets which are subject to a charge in favour of the trustee until the charge has been satisfied: *Vacuum Oil Co Pty Ltd v Wiltshire.*

1. Neither *Octavo Investments* nor *Vacuum Oil* examined the precise character of the interest in question, save for its beneficial proprietary character and its inuring for the benefit of the estate of the trustee (in insolvency in *Octavo Investments*). The nature of the right and interest has been the subject of consideration in the context of revenue statutes. In *Kemtron Industries Pty Ltd v Commissioner of Stamp Duties* [1984] 1 Qd R 576 McPherson J (with whom Andrews SPJ agreed) doubted whether it was a charge in the nature of an encumbrance, though he recognised that there was a property interest. McPherson J likened the interest to that of a partner in partnership assets. In *Buckle* 192 CLR 226, the Court approved McPherson J’s reasons in *Kemtron*, saying the following at 246-247 [48]-[51]:

48 … The entitlement of the beneficiaries in respect of the assets held by the trustee which constitutes the “property” to which the beneficiaries are entitled in equity is to be distinguished from the assets themselves. The entitlement of the beneficiaries is confined to so much of those assets as is available after the liabilities in question have been discharged or provision has been made for them [*Kentrom Industries Pty Ltd v Commissioner of Stamp Duties (Q)* [1984] 1 Qd R 576 at 587]. To the extent that the assets held by the trustee are subject to their application to reimburse or exonerate the trustee, they are not “trust assets” or “trust property” in the sense that they are held solely upon trusts imposing fiduciary duties which bind the trustee in favour of the beneficiaries [*Octavo Investments Pty Ltd v Knight* (1979) 144 CLR 360 at 370].

49 The entitlement to reimbursement and exoneration was identified by Lindley LJ as “the price paid by cestuis que trust for the gratuitous and onerous services of trustees” [*In re Beddoe* [1893] 1 Ch 547 at 558]. The right of the trustee has been described as a first charge upon the assets vested in the trustee [*Staniar v Evans* (1886) 34 Ch D 470 at 477], as one upon the “trust assets” [*Octavo Investments* 144 CLR 360 at 367. See also *Re Exhall Coal Co (Ltd)* (1866) 35 Beav 449 at 452-453 [55 ER 970 at 971]], and as conferring upon the trustee an “interest in the trust property [which] amounts to a proprietary interest” [*Octavo Investments* (1979) 144 CLR 360 at 370].

50 However, the starting point in the class of case under consideration is that the assets held by the trustee are “no longer property held solely in the interests of the beneficiaries of the trust” [*Octavo Investments* at 370]. The term “trust assets” may be used to identify those held by the trustee upon the terms of the trust, but, in respect of such assets, there exist the respective proprietary rights, in order of priority, of the trustee and the beneficiaries. The interests of the beneficiaries are not “encumbered” by the trustee’s right of exoneration or reimbursement. Rather, the trustee’s right to exoneration or recoupment “takes priority over the rights in or in reference to the assets of beneficiaries or others who stand in that situation” [*Vacuum Oil Co* at 335]. A court of equity may authorise the sale of assets held by the trustee so as to satisfy the right to reimbursement or exoneration. In that sense, there is an equitable charge over the “trust assets” which may be enforced in the same way as any other equitable charge [*Vacuum Oil* at 355]. However, the enforcement of the charge is an exercise of the prior rights conferred upon the trustee as a necessary incident of the office of the trustee. It is not a security interest or right which has been created, whether consensually or by operation of law, over the interests of the beneficiaries so as to encumber them in the sense required by s 66(1) of the [Stamp Duties Act.] In valuing the interests of beneficiaries which are conveyed by an instrument, there is no encumbrance which the Act requires to be disregarded.

51 Accordingly, we agree with the following treatment of the matter by Sheller JA [*Buckle* (1995) 38 NSWLR 574 at 586]

If it be right, as in my opinion it is, that the trustee has a beneficial interest in the trust assets to the extent of its right to be indemnified out of those assets against personal liabilities incurred in the performance of the trust and that interest will be preferred to the beneficial interests of the cestuis que trust, the consequence is that the interest conveyed has no value. This does not depend in any way upon treating the interest as encumbered. It flows from the fact that the trustee has a preferred beneficial interest in the trust fund.

1. The nature of the interest was once again discussed by the High Court in *CPT Custodian Pty Ltd v Commissioner of State Revenue (Vic)* [2005] HCA 53; 224 CLR 98. It is unnecessary to deal with the case in detail. It suffices to say that the Court emphasised the lack of precision in words such as “interest” and “property” which lack a universal contemporary or historical meaning, especially if there is a particular statutory context: *CPT Custodian* 224 CLR at 114 [31].
2. A trustee may exercise its right of indemnity without judicial intervention where property is not required to be sold: *Jennings v Mather* [1902] 1 KB 1 at 6; *Apostolou v VA Corp Aust Pty Ltd* [2010] FCA 64; 77 ACSR 84 at 92-93 [38]-[39]. But the lien does not confer a power of sale, and if sale be necessary a court order or the appointment of a receiver to sell is required: *Apostolou v VA Corp Aust Pty Ltd* [2011] FCAFC 103 at [45]; and see generally Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths, 2016) at 512-514 [21.04].
3. It is important to keep distinct the right of indemnity by way of reimbursement or recoupment, and the right by way of exoneration. To this end, I will refer to them as the right of reimbursement and the right of exoneration. It is important because there can be no doubt that if the trustee has used its own funds to pay the “trust debt”, the right of reimbursement is its personal asset which falls into its general estate without any attendant equitable obligation, and, if it happens to be insolvent, is available for all creditors, not limited to creditors of the trust in the sense of creditors of the trustee company acting in execution of the business of the trust. On the other hand, if the trustee has not paid the debt or liability from its own money before seeking to exercise the right (as it is not bound to: *In re Blundell* (1884) 40 Ch D 370 at 376-377; *Johnston v Salvage Association* (1887) 19 QBD 458 at 460; *Savage v Union Bank of Australia Ltd* [1906] HCA 37; 3 CLR 1170 at 1197) it is necessary to understand the precise nature of the right and its relationship with the creditors.
4. In *Ex parte Edmonds* (1862) 4 DeG F & J 488 at 498; 45 ER 1273 at 1277, Turner LJ said (in a passage cited by Dixon J in *Vacuum Oil* 72 CLR at 335-336):

The executor or trustee directed to carry on the business having the right to resort for his indemnity to the assets directed to be employed in carrying it on, the creditors of the trade are entitled to the benefit of that right, and thus **become creditors of the fund** to which the executor or trustee has a right to resort.

(emphasis added)

1. After citing this passage, Dixon J said the following in *Vacuum Oil* at 336:

But the creditors of the trade carried on by the executor must, as in all other cases of subrogation, depend upon his rights, and in that sense their claims upon the assets of the estate are indirect. This is well shown by the example of an executor who, through his wrongful act, has lost his right of indemnity or has disentitled himself to an indemnity except on terms of making good a loss to the estate. In such a case the creditors of his trade can have no better right [citing *In re Johnson* (1880) 15 Ch D at 552 and 555].

1. The above passages in *Scott* ([36] above), *Worrall v Harford* ([38] above) *Ex parte Edmonds* ([46] above) and *Vacuum Oil* ([47] above) identify the obligation of the trustee to the creditors and the nature of the trust institution as the source of the trustee’s right and interest and of the purpose of the right (to pay the creditors), and thus of the shape and content of the right. The right of the trustee to reach into the trust assets is not a personal right devoid of connection with the purposes and working of the trust; it inheres in, and arises out of, the trust relationship that exists for a purpose – to pay the creditors and thus to exonerate the trustee. It is without doubt a right of the trustee (and in that sense personal), but one that is constrained in its content by its purpose – the payment of trust creditors. In *In re Johnson* 15 Ch D at 552, Sir George Jessel MR with his customary clarity and unequivocality expressed the character of the right with its attendant obligation in equity to use the funds produced by the exercise of the right of exoneration to pay the creditors of the trust. His Lordship said:

I understand the doctrine to be this that where a trustee is authorised by a testator, or by a settlor … to carry on a business with certain funds which he gives to the trustee for that purpose, the creditor who trusts the executor has a right to say, “I had the personal liability of the man I trusted, and I have also a right to be put in his place against the assets; that is, I have a right to the benefit of indemnity or lien which he has against the assets devoted to the purposes of the trade.” The first right is his general right by contract, because he trusted the trustee or executor: he has a personal right to sue him and to get judgment and make him a bankrupt. The second right is a mere corollary to those numerous cases in Equity in which persons are allowed to follow trust assets. The trust assets having been devoted to carrying on the trade, it would not be right that the *cestui que trust* should get the benefit of the trade without paying the liabilities; therefore the Court says to him, You shall not set up a trustee who may be a man of straw, and make him a bankrupt to avoid the responsibility of the assets for carrying on the trade: the Court puts the creditor, so to speak, as I understand it, in the place of the trustee. **But if the trustee has wronged the trust estate, that is, if he has taken money out of the assets more than sufficient to pay the debts, and instead of applying them to the payment of the debts has put them into his own pocket, then it appears to me there is no such equity, because the *cestuis que trust* are not taking the benefit. The trustee having pocketed the money, the title of the creditor, so to speak, to be put in the place of the trustee, is a title to get nothing, because nothing is due to the trustee.**

(emphasis added)

1. At the core of what Jessel MR said was the proposition that the right (in a sense personal in that it was distinct from and superior to the interests of cestuis que trust) of the trustee to use trust assets to exonerate itself arises to meet a trust liability, and can be exercised only for that purpose. The property in the hands of the trustee remains trust property, but subject to the trustee’s proprietary interest that exists for the purpose of paying the creditors. The property is not held on trust for the beneficiaries alone; the proprietary interest of the trustee is preferential to the interests of the beneficiaries, but that interest of the trustee is shaped by its purpose and origins in the trust relationship – to pay trust creditors in order to exonerate itself from those debts. The character and limits of the interest are shaped by its purpose and origins. The obligation of the trustee to use the trust assets to pay trust creditors is reflected by, and provides the foundation for, the creditors’ right of subrogation.
2. To call something a proprietary interest does not conclude the enquiry into the nature of that interest. That a trustee has, in the sense discussed, a personal right which can be legitimately described as proprietary does not mean that it is the equivalent of unconstrained and general ownership.
3. If this is the proper way to view the matter, the following analysis flows naturally. If a company or person is a trustee of more than one trust or owns property in his, her or its own right as well as being a trustee of a trust, the trust assets, that is property impressed with a particular trust, can only be used for the purposes of that trust. So, if a trustee (not having used its own funds to pay a debt) reaches into the assets of the trust pursuant to a right of exoneration, it cannot use those funds for any purpose other than the payment of the debt from which the right was intended to exonerate the trustee. The trustee would be subject to a fiduciary duty to use the funds of the trust for trust purposes and for the purpose which gave rise to the entitlement – the payment of the creditor to whom the trustee was indebted. To use proceeds from the exercise of the right of exoneration to benefit itself personally would be to advantage itself at the expense of the trust. To use proceeds from the exercise of the right of exoneration to pay the creditor of another trust would be to use an asset impressed with one trust for the benefit of another trust.
4. The correctness of the proposition that the trustee is obliged by fiduciary duty to use the right of exoneration only to pay trust creditors is at the heart of this application. It is denied by the authority of the Full Court of the Supreme Court of Victoria in *Re Enhill*; it is supported by the approach of Needham J in *Re Byrne* and by the Full Court of the Supreme Court of South Australia in *In re Suco Gold*.
5. It is necessary to turn to *Octavo Investments*. It is important to appreciate what the Court in *Octavo Investments* 144 CLR 360 decided, and what it did not decide. Coastline Distributors Pty Ltd (**Coastline**) had paid up capital of five $1 shares, one share being held by each of its five directors who were also directors of Octavo Investments Pty Ltd (**Octavo**). A deed of trust settled $10 upon Coastline for the benefit of five companies owned by the directors as family trust companies. Coastline was authorised to carry on business on behalf of the trust. It carried on business as a distributor of frozen foods. The enterprise was not successful. Coastline was wound up in insolvency. In the months prior to liquidation (and within the preference period) Coastline made payments to Octavo of $49,750. The liquidators sought to have the payments declared void as preferences. The primary judge made such orders and the appeal to the Full Court was dismissed. There is no suggestion in the report that there was any more than one trust which had been trading; nor is there a suggestion that there were any creditors of Coastline other than creditors of the trustee in the proper carrying on of the business of the trust – that is trust creditors.
6. Section 293(1) of the *Companies Act 1961-1975* (Qld) provided for the application of s 122 of the *Bankruptcy Act 1966* (Cth) for the avoidance of preferences as follows:

Any transfer, mortgage, delivery of goods, payment, execution or other act relating to property made or done by or against a company which, had it been made or done by or against an individual, would in his bankruptcy be void or voidable shall in the event of the company being would up be void or voidable in like manner.

1. Section 122 of the *Bankruptcy Act* was, relevantly, in the following terms:

(1) A conveyance or transfer of property, a charge on property, a payment made or an obligation incurred by a person who is unable to pay his debts as they become due from his own money (in this section referred to as “the debtor”), in favour of a creditor, having the effect of giving that creditor a preference, priority or advantage over other creditors, being a conveyance, transfer, charge, payment or obligation executed, made or incurred –

(a) within six months before the presentation of a petition on which, or by virtue of the presentation of which, the debtor becomes a bankrupt; or

(b) after the presentation of a petition on which the debtor becomes a bankrupt and before the debtor becomes a bankrupt,

is void as against the trustee in the bankruptcy.

1. The views of the primary judge and the Full Court were summarised by Stephen, Mason, Aickin and Wilson JJ at 144 CLR 364-365, as follows:

The primary judge had little difficulty in coming to the conclusion that the payments in question gave Octavo a preference or an advantage over other creditors of Coastline and that, throughout the period in which the payments were made, Coastline was unable to meet its debts as they became due from its own money. He also concluded that the directors of Octavo had, at the very least, reason to suspect that Coastline was unable to pay its debts as they became due from its own money and that the effect of the payments to Octavo was to give that company an advantage over other creditors.

It followed from these findings that, provided s 122 of the *Bankruptcy Act* applied, Octavo was to be deemed not to be a payee in good faith within the meaning of s 122 (4) and the payments in question were void against the liquidator (s 122(1) and (2)). Both the trial judge and the Full Court were of the opinion that s 122 did apply to the facts of this case.

1. Thus, the company had creditors: all were trust creditors; the company was insolvent; it paid money to one creditor that gave it a preference or advantage over other creditors; and no defences applied.
2. Three arguments were put by the appellant Octavo (the preferred creditor). They are set out at 144 CLR 361-362 and 365-366. First, since all the property in Coastline’s hands was trust property, it did not come within the description of “property divisible amongst the creditors of the bankrupt” for the purposes of s 116 of the *Bankruptcy Act*. The legal estate in the property thus did not vest in the trustee. So, if the payments were somehow void the money would be repayable to the bankrupt trustee, not the trustee in bankruptcy. Since s 122 did not render preferences void as against a bankrupt, but only against a trustee in bankruptcy, s 122 had no application. Secondly, because the payments were made from trust funds, they were not made from Coastline’s “own money”, as that phrase appears in s 122. Thirdly, the liquidators were in truth complaining about the loss of Coastline’s right to an indemnity against that part of the trust assets comprised in the payments to Octavo, and such a right is not “property” within the meaning of that word in s 122. The release or surrender of a lien or charge by which the right of indemnity is secured was said not to be touched by s 122.
3. The central reasoning commences at 144 CLR 367 by stating relevant general principles: the trustee’s personal liability for debts incurred in the discharge of the trust: *Vacuum Oil*; the entitlement of the trustee to an indemnity against those liabilities from the trust assets; the possession by the trustee of a charge or right of lien over those assets to secure the entitlement: *Vacuum Oil*; and the lien applying to all trust assets, subject to the terms of the trust: *Dowse v Gorton* [1891] AC 190. These considerations led to the conclusion that both the cestuis quetrust and the trustee have beneficial interests in the trust assets, the latter’s interest being preferred to that of the former.
4. The Court then examined the position of the creditors. They were said to have “limited rights with respect to the trust assets”, having no right to take the assets in execution; but if the trustee is insolvent “the creditors will be subrogated to the beneficial interest enjoyed by the trustee.” The Court referred in this respect to *Savage* 3 CLR at 1186 (citing *Jennings v Mather* [1901] 1 KB 108, and on appeal [1902] 1 KB 1); *In* *re Morgan*; *Pillgrem v Pillgrem* (1881) 18 Ch D 93; *Vacuum Oil*; and *Ex parte Garland* (1804) 10 Ves Jun 110 at 120; 32 ER 786 at 789. Their Honours continued (at 144 CLR 367) as follows:

These principles lead naturally to the conclusion that the beneficial interests which, by subrogation, the creditors whose claims arise from the carrying on of the business have in the assets held by a bankrupt trustee form part of the property of the bankrupt divisible amongst his creditors.

For these propositions their Honours cited *Savage* 3 CLR at 1188, *Jennings v Mather* [1901] 1 KB at 116, and *Governors of St Thomas’s Hospital v Richardson* [1910] 1 KB 271.

1. This beneficial interest of the trustee, which through subrogation the creditors have, thus forms property which was held to be both “property” and “property of the bankrupt” for the purposes of the definitions of that word and that phrase in s 5 of the *Bankruptcy Act*:

“property” means real or personal property of every description, whether situate in Australia or elsewhere, and includes any estate, interest or profit, whether present or future, vested or contingent, arising out of or incident to any such real or personal property;

…

“the property of the bankrupt”, in relation to a bankrupt, means the property divisible amongst the creditors of the bankrupt and includes any rights and powers in relation to that property that would have been exercisable by the bankrupt if he had not become a bankrupt”.

1. The central argument in *Octavo Investments* relevant to this application is the first argument referred to at [58] above. It is in the resolution of this argument that the limits of what their Honours decided is to be appreciated. The interest of the trustee in the assets (by way of lien or charge) means that the cestuis quetrust are not entitled to call for the property. The Court said at 370:

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.**

(emphasis added)

1. Thus, s 116(2) was not engaged to exclude property from that divisible in the bankruptcy. Section 122 was engaged. The interest in the property that passed to the trustee in bankruptcy did so, however, for the benefit of trust creditors.
2. In the next paragraph (144 CLR at 370) their Honours considered the position of creditors:

The fact that the trust property itself cannot be taken in execution by the creditors of the trustee is not to the point. Those creditors are nevertheless subrogated to the rights of the trustee in relation to that property, and in the event of the trustee becoming bankrupt, **it is those rights which are to be realised in their favour.**

(emphasis added)

1. Once again, their Honours referred to the benefit to the trust creditors of the rights of the trustee in relation to the property. Again, however, it is to be recalled that all creditors were trust creditors and there was no call to distinguish between the right of reimbursement after a debt was paid, and the right of exoneration before the debt was paid.
2. At 144 CLR 370-371, their Honours discussed the debate as to whether the legal estate in the trust property over which the bankrupt trustee has a charge vests in the trustee in bankruptcy. Their Honours did not need to decide the question. The bankrupt trustee’s beneficial interest passed to the trustee in bankruptcy. That was sufficient to attract s 122. Their Honours said the following at 371 (remembering the context – all the creditors being creditors of the trust’s operations):

… Once it is recognised that a trustee may enjoy a right of indemnity over trust property in respect of liabilities incurred by him in the administration of the trust, it follows that the creditors of a trust business may have resort of the assets of the trust to the extent of the liabilities incurred by the trustee. Section 122 is apt in the case of an individual trading trustee to render void as against the trustee in bankruptcy a payment out of the trust property in circumstances which have the effect of giving the payee a preference, priority or advantage over other creditors.

1. Further, although the trustee’s right of indemnity (whether reimbursement or exoneration) can be taken to be a personal proprietary interest of the trustee taking priority over the interests of the beneficiaries, that says nothing about whether the interest is constrained or not or shaped in its content by an equitable obligation to use it to pay the trust creditors. Nor does the character and content of the right of the trustee mean that the right of exoneration is held on trust for creditors. In *In re Blundell; Blundell v Blundell* (1889) 44 Ch D 1 at 11, Lindley LJ said:

Creditors of the trustees in dealings carried on in pursuance of the trust are not cestuis que trust, but they have a right to the benefit of the right of the trustees to indemnity …

1. The entitlement of the creditors to be subrogated to the trustee’s right of exoneration out of the trust assets is derivative through the trustee. It does not give the creditors an interest as secured creditors or to a right of execution against trust assets. Nor does the trustee hold the right of indemnity on trust for the creditors. See also in this latter regard *Re McLernon* [1995] FCA 539; 58 FCR 391 at 406G. *Scott* describes the nature of the right of indemnity as the entitlement to bring a bill of equity to compel the exercise of the right of exoneration: *Scott on Trusts* (4th ed) at 468 (§ 268); and see *In re Raybould* [1980] 1 Ch 199 at 201-202. *Octavo Investments* makes it plain that the right is property of the trustee. In the hands of the liquidator the proprietary interest that derives from trust property is beneficially held by the trustee. It is its interest that takes priority over the interests of the beneficiaries. It is not held on trust for the beneficiaries; in that sense, it is not trust property standing outside the liquidation. It is not property held on trust for the creditors; it is property of the company but having its origins as trust property and, from its characteristics, is payable to creditors of the trust, the trustee’s personal liability to whom gave rise to its (the trustee’s) beneficial interest.
2. Once one appreciates that the trustee’s right of exoneration is a proprietary interest of the trustee that is held by the trustee in preference or priority to the beneficiaries’ interests, it cannot be considered as other than property of the company. Not only is that conclusion required by *Octavo Investments*, but also by *Buckle* 192 CLR at 246-247 [49]-[51] and *Bruton Holdings Pty Ltd (in liq) v Commissioner of Taxation* [2009] HCA 32; 239 CLR 346 at 359 [43]. The trust assets are not property of the company, but the trustee’s right of exoneration supported by the lien in the character of a proprietary interest is. It is, however, property of a particular character, with its content and shape determined by its origin as trust property, and the purpose for which it came into existence – the payment of creditors the liability to whom was incurred in executing the trust. These circumstances mark out the property (of the company) as limited. It is not trust property, but property of the company, the nature of which limits those who are to be paid from it.
3. In *Re Byrne* [1981] 1 NSWLR at 398, Needham J made the point that in *Octavo Investments* there were no creditors apart from trust creditors, and he said:

… there was certainly no suggestion that the “proprietary interest” which the trustee had in the trust fund was property divisible among the creditors other than those who were subrogated to the trustee’s right of indemnity. In other words, the case is not authority for the proposition that, where a trustee company carries on business with a trust fund and incurs liabilities and then is wound up, the whole of the trust fund is property divisible amongst all the company’s creditors, whether trust creditors or not. The right of indemnity arises only because the trustee is liable to creditors whose debts arose because of its activities as trustee of the fund. If there is no right of indemnity, there is no “proprietary interest”. For example, if a company, having various powers including a power to act as trustee, carries on business on its own account as well as in its capacity as a trustee, it would have no right of indemnity out of the assets of the trust for liabilities it incurred in the business it carried on on its own account, and the creditors of that business would have no right to look to the trust assets for payment of their debts by subrogation to the company’s rights.

1. In my respectful opinion, Needham J was correct in his identification of the limits of *Octavo Investments.*
2. *Re Byrne* was an application for directions brought by the liquidator as to the proper use of the proceeds of assets of a trading trust that had been carried on by the insolvent trustee. In particular, the question was whether the assets could be used for creditors other than trust creditors. The answer was no. The implicit foundation of Needham J’s approach was the attachment of the obligation to the trustee’s personal interest in its right of exoneration to use the right only for trust purposes.
3. At [1981] 1 NSWLR 399, Needham J adverted to the possibility of the operation of the statutory order of priority applying to differentiate between trust creditors, saying:

A question may arise, it seems to me, as to whether, in a case like the present, priority of one trust creditor over another in respect of the assets out of which the trustee was entitled to an indemnity is created by s 292; for example, whether, by virtue of s 292(1)(b), wages or salary of employees takes priority over trade creditors’ claims. No argument was directed to this possibility, as the two parties represented had no interest to argue the matter. It is a matter as to which I think counsel should consider whether a new representative party should be added. The High Court spoke of the trustees’ right of indemnity as coming within the definition of s 5 of the *Bankruptcy Act* of “property”. It could be suggested, therefore, that, in so far as there were different groups of creditors entitled to share in that “property”, the provisions of s 292(1) should apply to grant priority to one over another.

For the above reasons, I am of the opinion that the assets of the company should be utilised in the payment of those creditors who can properly be called trust creditors. If the liquidator wishes to submit that he is one of such creditors, then evidence should be filed to support such a claim and further argument can be had. Also, if counsel consider that the question of priority as between trust creditors is a live issue, an application should be made for the addition of another representative party, or perhaps, in the interests of economy, the liquidator could represent those groups who would claim priority.

1. In a subsequent hearing ([1981] 2 NSWLR 364), Needham J rejected the liquidator’s claim that he was a trust creditor, saying at 366 and 367:

The liquidator is not, in my opinion, administering the trust; he is winding up the company which, as trustee, has a liability towards the persons with claims against the trust property. The company is entitled to use the trust property to meet those claims because of its right to an indemnity. It could not be said, on this analysis, that the liquidator, in winding up the company, is administering the trusts of the settlement.

…

The liquidator’s remuneration must come out of the assets of the company; this company has no assets, but it has a right of indemnity against the assets of the trust to meet its obligation to pay creditors of the trust business. It is clear that the liquidator is not such. He is a functionary, in this case, appointed by the members and confirmed in office by the creditors, who has statutory powers and duties. He has a statutory right to remuneration and has a priority over other unsecured debts: s 292(1). If the creditors wished to ensure that the liquidator should have a right to look to assets other than the assets of the company for payment of his remuneration, they could not do so, in my opinion, merely by carrying out the procedures designed by the statute to ensure that the liquidator recovers, in a proper priority, his claim for costs and expenses out of the company’s assets. If as a body, or even as individuals or groups of individuals, they wish to ensure that distributions which would, in the proper course of events, come to them should be deferred to the claim of the liquidator, then no doubt they can take the necessary steps to ensure that result. My decision in this case is that the liquidator is not entitled to deduct his costs or expenses out of the trust assets.

1. In *Re Enhill*, Young CJ at [1983] VR 564 expressed the view that there was no limitation upon the expression of the matter in *Octavo Investments* that the right of indemnity was to be applied. The Chief Justice referred to *Jennings v Maher* [1901] 1 KB at 116-117 as support for the conclusion. With respect, to say that the right of exoneration is property of the trustee, does not answer the question whether it can be used for the benefit of all creditors. The essential reason why Young CJ said that it was solely personal property able to be used for any purpose was because it was for personal exoneration. The Chief Justice said:

In these circumstances to hold that a trustee in bankruptcy could only apply the proceeds of the right of indemnity towards some only of the bankrupt’s creditors, viz. creditors of the trust business, would deny the very purpose of the right to indemnity which is to exonerate the trustee’s personal estate.

1. With respect, the purpose is to be expressed somewhat more precisely. The purpose is the exoneration of the trustee’s personal estate **from trust obligations**. That personal, but qualified purpose, entitles the trustee to use trust property. A distinction was made by Young CJ at 564-565 where the trustee’s indemnity derives from a party who is concerned with the application of the money, referring to *Liverpool Mortgage Insurance Company’s Case* [1914] 2 Ch 617 at 633. Lush J at 567-569 also emphasised the personal nature of the trustee’s right. That conclusion carried with it the denial that there was any obligation, whether before or after insolvency, on the trustee to use trust funds to pay the trust debt. With respect, the nature of the personal interest in the right of exoneration is to use trust assets to alleviate a personal obligation entered into as trustee for trust purposes. It is a right arising from the trust relationship and in which creditors are interested as discussed in *Octavo.* With respect, I agree with the following passage from the judgment of King CJ in *In re Suco Gold* at 105 that was central to his disagreement with *Re Enhill*:

A trustee, however, has no legal right to use or apply the trust property other than for the authorised purposes of the trust. In particular he has no legal right to apply the trust property for his own benefit or for the benefit of third parties: *Keech v Sandford* [(1726 2 Eq. Cas. Abr. 741]). I cannot escape the conviction that if a trustee, or his trustee in bankruptcy, or liquidator in the case of a trustee company, is permitted to use trust property, not for the discharge exclusively of liabilities incurred in the performance of the trust, but in the discharge of other liabilities as well, the money is being used for an unauthorised purpose and is being used, moreover, for the benefit of the trustee, and of third parties, namely the non-trust creditors.

1. Chief Justice King then went on at 106-107 to discuss the possible conflict between *In re Richardson* [1911] 2 KB 705 and *Liverpool Mortgage Insurance Company’s Case* [1914] 2 Ch 617. I agree with King CJ’s analysis in that regard.
2. Chief Justice King’s views accord with principle. The nature of the right, personal in one sense, for the benefit of creditors in one sense, is, as the right of exoneration, necessarily shaped by the fact that it is over, or in respect of, trust property to be used for trust purposes. The right of indemnification passes to the insolvent estate of the trustee. If payment has already been made the right of recoupment is a generally available asset; if not, the right of exoneration is an asset available for trust creditors, unless a different conclusion is a result of statute.
3. The right of exoneration and the lien in its support are property of the company which is the trustee. One need go no further than *Octavo Investments* for that proposition. The creditors are not beneficiaries of a trust in which the right of exoneration is held on trust for them. It is the property of the trustee. But that does not mean that it is a proprietary interest unattended by inhering equitable obligation. Its nature and character are that it is exercisable only to pay trust creditors.
4. How then does the *Corporations Act* affect these principles?
5. Analysed in the way I have, the right of exoneration is property within the meaning of s 9 of the *Corporations Act*:

… [A]ny legal or equitable estate or interest (whether present or future and whether vested or contingent) in real or personal property of any description and includes a thing in action …

1. Upon the intervention of insolvency and the appointment of a liquidator, the liquidator takes control of the property of the company. That includes the assets of the trust for the purpose of indemnification – by recoupment or exoneration.
2. The question arises how the *Corporations Act* affects the use of the property now under the control of the liquidator as property of the company, being the right to use the trust assets for recoupment and exoneration.
3. It is convenient at this point to turn to the separate questions which were posed for the Court.

## Question 1: Did the liquidator have power to sell the trust assets by reference to the power in s 477 of the *Corporations Act*?

1. The disqualification of the Company to act as trustee meant that cll 7.27 and 7.28 (see [9] above) were not available to found the sale of assets. It was not submitted that, as a bare trustee at the most, the statutory power under s 27 of the *Trustees Act* was available. The right of exoneration and the proprietary right or lien supporting it were assets of the Company. I have discussed above the question of the nature of the lien and the proprietary interest in the trust assets that the right of the exoneration and the supporting lien create. It was submitted that the proprietary character of the right, together with the legal interest in the property was sufficient to engage s 477(2)(c) when read with s 477(2)(m).
2. In *Buckle*, the Court approved the reasons of McPherson J in *Kemtron*, and, whilst recognising the description of the interest as a first charge, said at 192 CLR 246-247 (see [42] above) that the trust assets, if there be an unsatisfied right of indemnity, are no longer held solely in the interests of the beneficiaries of the trust. The proprietary rights were, in order of priority, that of the trustee and then, thereafter, the beneficiaries. The interest of the beneficiaries was not “encumbered” by that of the trustee. Rather, quoting Dixon J in *Vacuum Oil* 72 CLR at 335, the Court said that the right of exoneration or recoupment “takes priority over the rights in or in reference to the assets of the beneficiaries or others who stand in that situation.”
3. Thus, in one sense, what exists can be seen to be an equitable proprietary interest or charge or lien in or over trust assets; but any enforcement by a Court of Equity is not of a security interest or a right created over the interests of the beneficiaries, but rather the enforcement by a Court of Equity of a prior proprietary interest in the trust fund to support the right of indemnity: see the words of Sheller JA in the Court of Appeal in *Buckle* 38 NSWLR at 586, specifically approved by the High Court in *Buckle* (see [42] above).
4. Section 477(2)(c) and (m) are in the following terms:

**477 Powers of liquidator**

…

(2) Subject to this section, a liquidator of a company may:

(c) sell or otherwise dispose of, in any manner, all or any part of the property of the company; and

…

(m) do all such other things as are necessary for winding up the affairs of the company and distributing its property.

…

1. It was submitted that the character of the right as somewhat more than a mere hypothecation or lien meant that the liquidator of a company was empowered by s 477(2)(c) when read with s 447(2)(m) to sell the interest and thus the underlying property. There are difficulties with this proposition. That the trustee’s interest in the property that is otherwise trust property (variously described over the years as a charge or lien or proprietary interest) inures to the trustee as its property does not mean that the trust asset can be sold without an order of the Court. The character of the trustee’s right is proprietary and can be seen as one to support the right of exoneration and has been described as an equitable lien. It arises from the trust relationship, a relationship which a Court of Equity will always supervise. The trustee’s interest is prior to the interest of the beneficiaries. To the extent that vindication of the trustee’s interest involves the sale of the underlying asset, there is every reason in legal policy to equate the rights of the trustee to sell the property (and, thus, of the liquidator of the former trustee to sell the property) to that of an equitable lien. Given the potential for interests of the beneficiaries to intrude in the sale (though not, on the facts here) the view expressed in *Apostolou*[2011] FCAFC 103 at [45] and in *Jacobs’ Law of Trusts in Australia* referred to at [44] above, has significant force. It will not always be the case that the trustee’s interest will exhaust the trust asset. If the trustee’s interest in the property is viewed as not including a power to sell the trust property without an order of the Court (as if it were an equitable lien) para (c) of s 477(2) is not apt to empower the liquidator to sell the underlying assets. Section 477(2)(c) should not be taken to refer to the sale or disposition of property which is not the property of the company, but which is trust property in which the trustee has a proprietary interest by way of interest or lien or charge to secure its right of exoneration. In such circumstances, the lien or charge is not being sold or disposed of, but the whole asset. It may well be that (as here) the size of the debt to the trust creditors is such that there will not be a relevant interest of the beneficiaries. That will not always be the case. Nevertheless, the assets that were held on trust are the subject of sale, not the right of exoneration or the lien or charge. I do not see para (m) of s 477(2) making any difference. Even with the wide meaning that should be given to that paragraph and in particular to the word “necessary”(“all such other things as are necessary for winding up the affairs of the company and distributing its property”): *Re* *Dallhold Investments Pty Ltd* [1994] FCA 738; 53 FCR 339 at 343-344 and the cases there cited, I do not see that the power to deal with the assets of the company – the lien or charge or proprietary interest of the trustee to secure the right of exoneration – authorises the liquidator to exercise the lien and sell the underlying assets which had been held on trust for the beneficiaries.
2. On the other hand, if the company to which the liquidator has been appointed remained a trustee “the affairs of the company” for the purposes of s 477(2)(m) would include administering the trust: *Re Crest Realty Pty Ltd (in liq) (No 2)* [1977] 1 NSWLR 664.
3. The nature of the property as an equitable lien or charge means that there is the need for an order of the Court to sell the trust property under the control of the liquidator and in and over which the lien or charge subsists. In the present circumstances, where there appears to be no issue but that the right of exoneration exhausts the trust property, the liquidator holding as he does the property and the equitable lien or charge could be given power to sell the property without the need to be appointed a receiver to hold trust property for the benefit of beneficiaries after exhaustion of the right of exoneration. The proceeds of sale can then be dealt with by the liquidator (as the product of the exercise of the right of exoneration) in accordance with the *Corporations Act* in the manner and for the reasons set out in answering question 2 below. It is unlikely that there would be any reason why the Court would not make such an order, here, nunc pro tunc, permitting the sale of trust assets.
4. In my view, question 1 should be answered: “No”.

## Question 2: Are either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds to be applied by the Plaintiff in accordance with the priority regime established by sections 555, 556, 560 and 561 of the *Corporations Act*?

### The unfair preference proceeds

1. The parties before us were agreed that the proceeds of the unfair preference action should be treated in accordance with the statutory priority regime. There is both reason and authority in favour of this approach: *NA Kratzmann Pty Ltd v Tucker (No 2)* [1968] HCA 44;123 CLR 295 at 300-301; *Re Fresjac Pty Ltd* (1995) 65 SASR 334 at 343-347; *Cook v Italiano Family Fruit Company Pty Ltd* [2010] FCA 1355; 190 FCR 474 at 478-489 [10]-[62]; but see *Jacobs’ Law of Trusts* (8th ed) at 524 [21-16] to the contrary.
2. In the light of the lack of argument, I would be content to adopt the position of the parties, but not to undertake any legal analysis. The answer given in this regard therefore comes from the acceptance of the position by all interested in the litigation.

### The realisation of the Trust Assets

1. On the clear authority of *Octavo Investments*, *Buckle* and *Bruton*,the proprietary interest of the trustee in the assets otherwise held on trust in support of the right of indemnity is property of the company. Its exercise may require the leave of the Court, involving the sale of trust property. The impressed character of the property becomes relevant upon the exercise of the right of exoneration. The proceeds of such exercise (leaving to one side the need for separate permission from the Court) cannot have any different character: as property of the company but constrained in nature and character for the reasons expressed above. That character is reflected in the obligation upon the liquidator to pay the funds to the creditors of the trust. That obligation reflects the right of subrogation described in *Octavo Investments* at 370 ([63] above). That subrogation and the obligation on the liquidator is (at least in circumstances of insolvency, though not necessarily so limited) a collective entitlement of all creditors: *Mason v Pomeroy* 24 NE 202 at 204 (1890) (Supreme Judicial Court of Massachusetts); Story J, *Commentaries on Equity Pleading* (7th ed, Little Brown, 1865) at 103-106 [99]; and *In re Raybould.*
2. The relevant provisions of the *Corporations Act* are ss 501, 555, 556, 560 and 561. It is unnecessary to set them out exhaustively here.
3. None of the relevant provisions of the *Corporations Act* purports to change the nature and character of the property that falls under the control of the liquidator as property of the company, or of the results of or proceeds from the exercise of that property.
4. Section 501 is directed to the pari passu distribution of property. It does not say and should not be taken as saying that property which of its nature and character is only able to be distributed among some creditors (pari passu) must be distributed to non-trust creditors.
5. Likewise, neither s 555, which provides for the equal ranking of debts, nor s 556, which provides for an order of priority for certain creditors, is concerned with changing the character of the property of the company. Nevertheless, there is no reason why their plain terms should not be read in the context of an understanding by Parliament that corporations can act from time to time as trustees of one or more trading trusts.
6. In *In re Suco Gold*, King CJ applied the statutory order of priorities to assets under the control of the liquidator. His Honour’s reasons can be seen at 33 SASR 107-110. In the circumstances before him, the insolvent company had been trustee of more than one trust, but had not carried on business on its own account. Thus, all liabilities had been incurred in the course of performing the trusts. The only assets of the insolvent trustee were the various rights of indemnity (exoneration) against the property of each trust. The Chief Justice said at 107-110:

It was argued, following the reasoning in *Re Enhill Pty Ltd*, that the proposition affirmed by the High Court in *Octavo’s* casethat the trustee’s right of indemnity is a beneficial interest in the trust property which passes to the trustee in bankruptcy or liquidator, leads to the conclusion that the trust assets, to the extent of the trust liabilities, pass to the trustee in bankruptcy or liquidator for the benefit of the general body of creditors. I do not think that *Octavo’s* caseleads to that conclusion. The right of indemnity, it is true, exists for the trustee’s own benefit and it passes to the trustee in bankruptcy or the liquidator. The proceeds of that right of indemnity are therefore part of the estate divisible among the creditors. It seems to me, however, that the right of indemnity can only produce proceeds for division among the creditors generally if the trustee has discharged the liabilities incurred in the performance of the trust and is therefore entitled to recoup himself out of the trust property. If he has not discharged the liabilities, the right of indemnity entitles him to resort to the trust property only for the purpose of discharging those liabilities. He may apply the trust moneys directly to the payment of the trust creditors or he may take it into his own possession for that purpose. If he takes trust property into his possession to satisfy his right to be indemnified in respect of unpaid trust liabilities, it seems to me that that property retains its character as trust property and may be used only for the purpose of discharging the liabilities incurred in the performance of the trust. The exercise of the right of indemnity is for the benefit of the trustee in that it relieves him of liability for the trust debts. If the trustee is bankrupt, or being a company is in liquidation, the trustee in bankruptcy or liquidator can exercise the right of indemnity which vests in him as part of the property of the bankrupt or insolvent company. If the trust liabilities have been discharged, the trustee in bankruptcy or liquidator is entitled to recoup the bankrupt estate out of the trust property and the proceeds of the right of indemnity become part of the property divisible among the creditors. If the liabilities have not been discharged, the trustee in bankruptcy or liquidator may, by reason of the right of indemnity which vests in him, apply the trust property to the payment of the trust liabilities, thereby exonerating the bankrupt estate to the extent of the value of the available trust assets. In the latter circumstances there cannot be proceeds of the right of indemnity which are available for distribution among the general body of creditors.

…

This view of the implications of the decision in *Octavo’s* case is confirmed by the emphasis which was placed in that case upon the right of the unpaid trust creditors to be subrogated, upon the bankruptcy or liquidation of the trustee, to the trustee’s right of indemnity. On bankruptcy or liquidation, the unpaid trust creditors are entitled to stand in the shoes of the trustee and to obtain payment from the trust property. Such a right is, in my view, inconsistent with the notion that the trust property is, to the extent of the trust liabilities, property of the bankrupt divisible among the general body of creditors. The existence of the right of subrogation must mean that the trust property, to the extent of the trustee’s right of indemnity, in respect of the unpaid trust liabilities, must be applied in payment of the trust creditors. Indeed this was made explicit in the joint judgment in *Octavo’s* case where the following passage appears at p. 91: “Those creditors are nevertheless subrogated to the rights of the trustee in relation to that property and in the event of the trustee becoming bankrupt, it is those rights which are to be realised *in their favour.*” (Italics mine).

…

How then are these principles to be applied in the present case? The company traded as trustee of two distinct trusts. All its liabilities were incurred in the course of performing those trusts. Its only assets are the rights of indemnity against the property of each trust. They are, of course, distinct rights of indemnity and therefore distinct assets. One such asset is the right of the company to be indemnified out of the assets of Daisy-Milano Goldfields Unit Trust in respect of liabilities incurred in the performance of that trust. The other is the right of the company to be indemnified out of the assets of Santa Claus Goldfields Unit Trust in respect of liabilities incurred in the performance of that trust. The liquidator is bound by the provisions of s 292 with respect to the payment of the company’s debts. He must therefore endeavour to pay the debts in accordance with the order of priority set out in that section. To the extent that each priority debt has been incurred in the performance of a particular trust he should have recourse to the property of that trust for the purpose of paying it. If there is a residue of assets of a particular trust after payment of the priority debts incurred in the performance of that trust, that residue should be applied to the payment of the other debts applicable to that trust. If there is a deficiency in the assets of a particular trust, the non-priority debts applicable to that trust would have to rank *pari passu*. The unpaid balance would, of course, rank for dividend out of the general assets of the company, but as there are no such assets that is an academic consideration.

1. I respectfully agree with the approach of the Chief Justice. Underlying it is the conclusion that the statute applies, in its terms, and applies to the funds produced from the exercise of the rights of exoneration (if more than one) differentially, recognising the limitations on those funds, deriving from the limitation on or character of the property that gave rise to them. This is to be justified, and is supported, in my view by the way one reads and applies the statute. The *Corporations Act* should not be restricted to its application to only some types of property of the company. Nor should it be construed as intended to change the nature of property of the company. In the well-known context of companies that act and carry on business on their own account and also as trustees for “business” trusts and in the context of well-known and fundamental equitable principles, the statute should be read and understood as applicable to corporations and their property of all kinds. That does not mean, however, that rights, duties and proprietary characteristics from the operation of well-known and fundamental principles should not be accommodated in the operation and working of the statute. Such rights, duties and characteristics are part of the legal groundwork and foundations against which one reads and applies the statute: the equitable principles and norms in which the statute was intended to operate.
2. Each of the provisions of s 556 has its own underlying legal policy and its own terminology. The analysis is easiest where the company has only ever acted as here as corporate trustee for one trust. In such circumstances, the property of the company that includes the right of exoneration and the funds obtained from its exercise is to be distributed in accordance with the statutory command: ss 501 and 556. In such circumstances, the words of the statute are to be applied to direct the distribution of the property of the company.
3. Complications arise where the company has administered more than one trust or has conducted affairs in its own right. In such circumstances, equitable principle may be necessary to supplement the operation of the statute without contradicting it. In such circumstances, the approach in *In re Suco Gold* treats the liquidator as holding more than one fund, each of which is directed to different groups of creditors. That is not because property of the company is not being applied in satisfaction of liabilities equally (s 501) or that debts and claims were not being taken to rank equally (s 555) but because the limited nature of the asset, the inhering characteristics of the proprietary interest, led to that outcome. Such an approach conforms with the recognition of the proprietary character of the asset of the company, its limited character, and the operation of the *Corporations Act* in the known context of trading trusts and well-known equitable principle.
4. In these circumstances, each provision in s 556 must be examined for its meaning. For instance s 556(1)(b) and its application may raise the question as to which fund should bear these costs – the relevant trust in respect of which the obligation was undertaken, or the general assets, or the trusts and the general assets rateably. These complexities do not arise here because there only ever was one activity (of one trust) and it was a voluntary winding up.
5. When dealing with the liquidator’s costs, King CJ concluded that they were payable out of the trustee’s right of indemnity. At 110, he said:

It seems to me that that course can be justified by reference to the obligations of the trustee company arising out of the carrying on of the business authorised by the trusts. It is part of the duty of the trustee company to incur debts for the purposes of the trust businesses and, of course, to pay those debts. Upon winding up those debts can only be paid in accordance with the provisions of the *Companies Act*. This requires necessarily that there be a liquidator and that he incur costs and expenses and be paid remuneration. Section 292 provides that there be paid the costs and expenses of winding up, the taxed costs of the petitioner and the remuneration of the liquidator “in priority to *other* unsecured debts”. The expression “*other* unsecured debts” appears to imply that the costs and expenses of winding up, the petitioner’s costs and the liquidator’s remuneration are regarded by the statute as debts of the company. As the company’s obligation as trustee to pay the debts incurred in carrying out the trust cannot be performed unless the liquidation proceeds, it seems to me to be reasonable to regard the expenses mentioned above as debts of the company incurred in discharging the duties imposed by the trust and as covered by the trustee’s right of indemnity.

…

On these principles which I have discussed, the liquidator is entitled to have recourse to the property of each trust for the purpose of meeting the costs and expenses of winding up, the petitioner’s costs and the liquidator’s remuneration, so far as they are incurred in relation to each trust. As there are no non-trust assets or liabilities, all the expenses are attributable to one or other of the trusts and must be apportioned between them. The liquidator will be able to make an estimate of the work and expense involved in the liquidation so far as it relates to each trust. Where no apportionment is possible, the maxim that equality is equity should provide the solution to the problem of apportionment.

(emphasis in original)

1. If I may respectfully say so, there is not only practical wisdom in this approach, but also a sufficient grounding in the terms of the statute. Whilst one cannot take too much from the legal context of the jurisprudence (especially given its lively currency), by the time of the passing of the *Corporations Act* in 2001 *In re Suco Gold* had been decided for over 17 years. The position was broadly that *In re Suco Gold* was both well-regarded and followed (though by no means universally) including in relation to priorities and liquidator’s costs. As to priorities and liquidator’s costs: *Re ADM Franchise Pty Ltd* (1983) 7 ACLR 987 (McLelland J); *Re Indopal Pty Ltd* (1987) 12 ACLR 54 (McLelland J); *Re GB Nathan and Co Pty Ltd (in liq)* (1991) 24 NSWLR 674 (McLelland J); *Sjoquist v Rock Eisteddfod Productions Pty Ltd* (1996) 19 ACSR 339 (McLelland J); and *13 Coromandel Place Pty Ltd v C L Custodians Pty Ltd (in liq)* (1999) 30 ACSR 377 (Finkelstein J). It should be noted, however, that some leading texts and commentators do not favour the order of priority solution in *In re Suco Gold*, though the rejection of *Re Enhill* is almost universal, except in Victoria: see Meagher RP and Gummow WMC, *Jacobs’ Law of Trusts in Australia* (5th ed, Butterworths, 1986) at 594-595; Heydon JD and Leeming MJ, *Jacobs’ Law of Trusts in Australia* (8th ed) at 522-523; McPherson BH, “The Insolvent Trading Trust” in Finn PD (ed), *Essays in Equity* (Lawbook Co, 1985) at 153-154.
2. I do not see equitable principle or any of the provisions of the *Corporations Act* as preventing the approach identified by King CJ, based as it is upon the limited nature of the proprietary interest of the insolvent trustee – to exonerate itself for a purpose out of trust property. Indeed, I see the legislation being given full effect, but harmoniously with fundamental equitable principle that otherwise governs and dictates the fair and proper administration of trusts, and into the framework and operation of which the statute was placed.
3. Turning, for instance, to s 556(1)(e), (f), (g) and (h), in the present factual and historical circumstances of the Company there is no reason why the words of the provision should not be applied. These provisions reflect, as do the balance of s 556, important public policy considerations of the legislature. The carrying on of business by trusts has been well known for many years before 2001. The Report of the Australian Law Reform Commission (No 45) on General Insolvency recommended express clarification of the statute that was broadly conformable with the approach of King CJ in *In re Suco Gold.* (See Report 45 Vol 1 at [265] and Ch 6, generally, and Vol 2 Appendix A Section D, being draft legislation on Corporate Trading Trusts.) The Parliament has not seen fit to make any particular clarification of the position of insolvent corporations that acted as trustees of trading trusts. That circumstance does not, however, reflect a Parliamentary rejection of *In re Suco Gold*; nor does it undermine the application of the words of the statute to property of the company, albeit of a particular character, to the extent conformable with principle. Where the corporation has only ever acted as a trustee of one trust and that has been the totality of its affairs, there is no reason either in principle or by reference to context or text why the words of the statute setting the order of priorities should not be followed. Complexities may arise in circumstances of multiple trusts or of trusts and activity on the corporation’s own account. Considerations of, or akin to, marshalling or hotchpot may be relevant as to the payment of debts dealt with in the statutory order. But these complexities will be resolved by application of principle and the text of the legislation, in a manner reflected by the approach of King CJ in *In re Suco Gold.*
4. Thus, in my view, question 2 should be answered: “Yes as to both”.

## Question 3: Should the Plaintiff be directed under s 511 of the *Corporations Act* to deal with either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds as assets in the winding up of the Company?

## Question 4: Alternatively, should the Plaintiff be directed under s 511 of the *Corporations Act* that either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds be distributed by the Plaintiff to unsecured creditors of the Trust pari passu after providing for the costs of administration (including the Administrators’ and Liquidators’ remuneration and expenses) only?

1. It follows from the above that question 3 should be answered “Yes as to both” and question 4 should be answered “No”.
2. I have had the benefit of reading the reasons of Farrell J. If I am wrong in the above view as to the meaning and operation of the *Corporations Act*, and if the distribution of the funds that are the product of the exercise of the right of exoneration is to be in accordance with equitable principle, then there is a sound basis to conclude that Equity would follow the statute by providing for the priority of employees. This way of approaching the matter was dealt with by the Commonwealth in [59] of its submissions. The following is a proper basis for the acceptance of that submission. The matter was not, however, squarely addressed and if it be the basis for decision as to distribution of the proceeds of the right of exoneration a full opportunity should be given for that debate.
3. The protection of employees in the aftermath of the insolvency of businesses is, and has been for many years, a matter of high public policy. The vulnerability of those who work in an employment relationship to the financial consequences of the decisions of business controllers and the economic environment is well-known. It has been consistently addressed in terms of priority in access to funds and latterly by a qualification to the reach and operation of securities over the assets of the business enterprise. That statutory addressing of the question as a Parliamentary response has been informed by considerations of the protection of the vulnerable and of fairness in the operation of the insolvency regime. Such considerations are basal to the very nature and operation of Equity as a body of principle (including, but not limited to, rules). As Lord Stowell said in *The Juliana* (1822) 2 Dods 504 at 522; 165 ER 1560 at 1567 in comparing the technique of Equity to that of the common law, “a court of equity takes a more comprehensive view, and looks to every connected circumstance that ought to influence its determination upon the real justice of the case.” This passage from an Admiralty suit was cited by Dixon CJ, McTiernan and Kitto JJ in *Jenyns v Public Curator (Queensland)* [1953] HCA 2; 90 CLR 113 at 119, because equity lay (and still lies) at the heart of maritime and Admiralty law.
4. The order of priorities to limited funds in any given situation is based on legal policy, especially justice and fairness. That a pari passu approach is generally applied is a reflection of Equity’s insistence on fairness and justice, through equality. Equality is Equity. But that maxim is not to be divorced from its informing source or values. The application of Equity by its adjustment of the maxim in the context of a statute of high public policy can be seen as the accommodation of equitable principles to the circumstances of the case to vindicate its fundamental norms of fairness, justice and equality, influenced by the recognition of a statute that reflects the cognate norm of the protection of the vulnerable.
5. By way of analogous comparison, the law of priorities of lien holders in Admiralty is subject to a degree of flexibility dictated by the imperative to do justice: *The Ruta* [2000] 1 Lloyd’s Rep 359; Thomas DR, *Maritime Liens* (Stevens, 1980) at [418]. This derives from the deep influence of equity in maritime law: see generally Tetley W, *International Maritime and Admiralty Law* (Edition Yvon Blais, 2002) at 54-56.
6. Just as equity deeply informs maritime and Admiralty law, so do the principles of Equity inform corporations law and the law of insolvency, notwithstanding the presence of detailed statutes in those areas.
7. Here, in the context of the protection of employees, there is every reason for Equity to follow the statute in applying its principles of distribution concerning employees conformably with the public policy in the statute which conforms with all of the relevant underlying norms of Equity: fairness, justice, the protection of the vulnerable and, within that framework, equality.
8. This approach might be seen as an example of consistent and clear legislative policy informing a change to judge-made law. In *Erven Warnink BV v J Townend & Sons (Hull) Ltd* [1979] AC 731 at 743, Lord Diplock said:

Nevertheless the increasing recognition by Parliament of the need for more rigorous standards of commercial honesty is a factor which should not be overlooked by a judge confronted by the choice whether or not to extend by analogy to circumstances in which it has not previously been applied a principle which has been applied in previous cases where the circumstances although different had some features in common with those of the case which he has to decide. Where over a period of years there can be discerned a steady trend in legislation which reflects the view of successive Parliaments as to what the public interest demands in a particular field of law, development of the common law in that part of the same field which has been left to it ought to proceed upon a parallel rather than a diverging course.

1. In 1937, Cardozo J, speaking for the Supreme Court, spoke of legislative policy as “a new generative impulse”: *Van Beeck v Sabine Towing Co* 300 US 342 at 351 (1937).
2. The same influence and approach can be seen in other cases: *Universe Tankships Inc of Monrovia v International Transport Workers Federation* (*The Universe Sentinel*) [1983] 1 AC 366 at 385; *Moorgate Tobacco Co Ltd v Philip Morris Ltd (No 2)* [1984] HCA 73; 156 CLR 414 at 445; *R v L* [1991] HCA 48; 174 CLR 379 at 390; *Moragne v States Marine Lines Inc* 398 US 375 at 390 (1970); *Esso Australia Resources Ltd v Commissioner of Taxation* [1999] HCA 67; 201 CLR 49 at 61-63 [23]-[28]; *Vadasz v Pioneer Concrete SA Pty Ltd* [1995] HCA 14; 184 CLR 102 at 115-116; *South Pacific Manufacturing Co Ltd v New Zealand Security Consultants & Investigations Ltd* [1992] 2 NZLR 282 at 298 and the cases cited thereat.Also, see the discussion of these and other cases by Gummow J, “The Common Law and Statute” in *Change and Continuity: Statute, Equity and Federalism* (Oxford, 1999) at 11-18; by Finn J, “Statutes and the Common Law” (1992) 22 *UWA LR* 7 and “Statutes and the Common Law: The Continuing Story” in Corcoran S and Bottomley S (eds) *Interpreting Statutes* (Federation Press, 2005) at 52; and by Leeming JA in “Equity: Ageless in the ‘Age of Statutes’” (2015) 9 *Jo of Equity* at 108, esp 124-128. Whilst the Court in *Lamb v Cotogno* [1987] HCA 47; 164 CLR 1 at 11-12 somewhat “discountenanced” (to quote Gummow J at 11 of the article cited above) the general proposition of statutory influence over general law as propounded by scholars such as Pound and Atiyah (“Common Law and Legislation” (1908) 21 *Harv LR* 383; and “Common Law and Statute Law” (1985) 48 *Mod LR* 1), their Honours did recognise the attenuated version in *Warnink*.
3. Here, the consistent policy of Parliaments discussed in the reasons of Farrell J has been to protect employees. The techniques have become progressively stronger, brought about by an appreciation of inadequacy in some circumstances of an earlier regime. There is, however, clear and consistent policy now based in national legislation. Equitable principle should reveal consistency with, not divergence from, public policy of such strength and consistency, when it conforms so completely with all the norms that underlie Equity.

## The orders of the Court

1. This paragraph expresses the views of all members of the bench. The orders of the Court are answers to the questions before the Court. For the reasons given by the members of the Court, the answers to the questions are as follows:

**Question 1:**

Are the assets of the Thompson Family Trust (**Trust**) as at the time of the resolution to wind up the Company (including the proceeds of sale of those assets) (**Trust Assets**) assets in the winding up of Killarnee Civil & Concrete Contractors Pty Ltd (In Liquidation) ACN 085 230 586 (**Company**) so that the liquidator had the power under section 477 of the *Corporations Act 2001* (Cth) to sell the Trust Assets?

**Answer 1:**

Each member of the Court answers “no”.

 **Question 2:**

Are either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds to be applied by the Plaintiff in accordance with the priority regime established by sections 555, 556, 560 and 561 of the *Corporations Act*?

**Answer 2:**

As to the unfair preference proceeds, each member of the Court answers “yes”, with the qualification set out in [93]-[94] of the reasons of the Chief Justice, agreed in by Justice Siopis at [149] and by Justice Farrell at [199].

As to the realisation of the Trust Assets, the Chief Justice and Justice Farrell answer “yes”, but for the different reasons set out in their reasons for judgment; and Justice Siopis answers “no”.

**Question 3:**

Should the Plaintiff be directed under s 511 of the *Corporations Act* to deal with either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds as assets in the winding up of the Company?

**Answer 3:**

The Chief Justice answers the question “yes as to both”; Justice Siopis answers the question “yes” as to unfair preference proceeds, but “no” as to the realisation of trust assets; and Justice Farrell answers to the effect that directions should be given in accordance with the answer to question 2, which is in substance the same answer as the Chief Justice.

**Question 4:**

Alternatively, should the Plaintiff be directed under s 511 of the *Corporations Act* that either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds be distributed by the Plaintiff to unsecured creditors of the Trust pari passu after providing for the costs of administration (including the Administrators’ and Liquidators’ remuneration and expenses) only?

**Answer 4:**

Each member of the Court answers “no”, but the Chief Justice and Justice Farrell reach that answer for reasons different to those of Justice Siopis.

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| --- |
| I certify that the preceding one hundred and twenty-one (121) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Chief Justice Allsop. |

Associate:

Dated: 21 March 2018

REASONS FOR JUDGMENT

SIOPIS J:

1. I have had the very considerable benefit of reading the draft reasons for decision of each of Allsop CJ and Farrell J.
2. Allsop CJ has set out in detail the factual background and the questions which the Court has been asked to answer. This relieves me from having to do so.

## Question one

1. I agree for the reasons given by Allsop CJ that the answer to question one is “No”.
2. I would, however, add the following.
3. Killarnee Civil & Concrete Contractors Pty Ltd (in liq) (the Company) is, and was in January 2015 to May 2015, when the liquidators, then comprising the current liquidator, Mr Martin Jones, and two former liquidators, sold trust assets comprising plant and equipment and a crane, no more than a bare trustee. Therefore, the Company, and so also the liquidators, did not have the power to sell trust assets.
4. There is other trust property which is still in the control of the current liquidator. This includes plant and equipment and a property located at Mardie Road, Karratha, Western Australia, which neither the Company nor the liquidator has the power to sell.
5. Recently the Court of Appeal of Victoria (the Court of Appeal) has given judgment in the case of *Commonwealth of Australia v Byrnes and Hewitt* [2018] VSCA 41 (*Byrnes*). The facts in that case are somewhat different to the facts in this case.
6. In that case, a company, Amerind Pty Ltd (Amerind), was appointed as trustee of a trading trust, and carried on business in that capacity. Amerind did not carry on any other business. Amerind entered into a secured facility with the Bendigo and Adelaide Bank Limited (the bank).
7. In March 2014, following a notice from the bank demanding repayment of monies owed by Amerind under the secured facility, the sole director of Amerind appointed administrators to Amerind.
8. On the same day, the bank appointed Mr Matthew Byrnes and Mr Andrew Hewitt as receivers and managers of Amerind. The receivers and managers continued to trade for about a month after their appointments, but then went into “wind down mode” and sold Amerind’s remaining stock. After the receivers and managers repaid the bank the amounts due to it, there was a surplus of monies.
9. On 13 August 2014, the creditors of Amerind resolved that Amerind be wound up. The creditors were all trust creditors in the sense that they had supplied goods and services to Amerind in its capacity as trustee carrying on the business of the trust. The trust creditors included employees.
10. The receivers and managers sought directions from the Court as to how the surplus of $1,619,018 which they continued to hold, should be distributed.
11. Section 433 of the *Corporations Act 2001* (Cth) relevantly provides:

(3) In the case of a company, the receiver or other person taking possession or assuming control of property of the company must pay, out of the property coming into his, her or its hands, the following debts or amounts in priority to any claim for principal or interest in respect of the debentures:

(a) first, any amount that in a winding up is payable in priority to unsecured debts pursuant to section 562;

…

(c) subject to subsections (6) and (7), next, any debt or amount that in a winding up is payable in priority to other unsecured debts pursuant to paragraph 556(1)(e), (g) or (h) or section 560.

1. A primary issue before the Court of Appeal was whether the surplus monies in the hands of the receivers and managers should be distributed among the trust creditors according to the statutory priority regime set out in s 556 of the *Corporations Act*.
2. The Court of Appeal held at [281] that once it was accepted that the trustee’s right of exoneration was the property of Amerind then s 555 and s 556 applied to the distribution of the surplus monies to the trust creditors.
3. The facts and circumstances of *Byrnes* are different in a material respect from the facts and circumstances of this case. This is because in *Byrnes* there was no suggestion that when the receivers and managers sold the trust assets they did not have the power to do so. Presumably, the assets were sold by the receivers and managers exercising powers of sale under the security instruments, and under the trust deed which appointed Amerind as trustee. Further, the receivers and managers obtained court directions confirming that they were justified in selling the trust assets.
4. In this case, however, by the time the then liquidators sold the trust assets, the Company had been removed from its position of trustee and the liquidators had no authority to sell the assets of the trust.
5. Accordingly, the only basis upon which the Company could sell the trust assets was in reliance upon its equitable lien, and that required intervention of a court exercising equitable jurisdiction to affect a judicial sale or to appoint a receiver to carry out the sale and the distribution of the proceeds. It is common cause that the then liquidators did not apply to a court for equitable intervention before they sold the trust assets during the period January 2015 to May 2015.
6. In my view, however, on the application of the liquidator (and the former liquidators) to the Court it is likely that, on the evidence, the Court will *nunc pro tunc* grant relief to the then liquidators in respect of the unauthorised sale of the assets during the period January 2015 to May 2015. The same is true in relation to the proposed sale of the other yet unsold trust assets held under the control of the liquidator.
7. It is relevant to identify the basis in law upon which a court would grant such relief and the nature of that relief.
8. It is accepted that the right of indemnity in respect of a trustee’s right of exoneration and the accompanying equitable lien will continue in favour of a company in liquidation which has incurred liabilities in carrying out trust business, notwithstanding that the company has been removed as trustee of the trust and only holds the trust assets as a bare trustee (*Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* (2008) 74 NSWLR 550). The company, through its officer, the liquidator, may rely upon the equitable lien to approach the court to authorise the sale of trust assets by way of equitable execution for the purpose of paying the trust creditors and so vindicating its right to exoneration, notwithstanding that it is a bare trustee. The usual way in which this is done is by the liquidator of the insolvent former corporate trustee asking the court to appoint a receiver for the purpose of selling the trust assets and distributing the proceeds among the trust creditors. In most cases, it is the liquidator who is appointed as the receiver for the purposes of selling the trust assets and distributing the proceeds to trust creditors.
9. For example, relief was relevantly granted in these circumstances, on the application of a liquidator, Mr Michael Smith, in the following terms by Brereton J in *Re Stansfield DIY Wealth Pty Limited (in liq)* (2014) 291 FLR 17:

The Court further orders that:

…

(4) Michael John Morris Smith of Smith Hancock, Level 4, 88 Phillip Street, Parramatta, Accountant and Insolvency Practitioner, be appointed without security as receiver and manager (the “Receiver”) of the assets and undertaking of the Super Fund until further order.

(5) The Receiver have the powers in the Schedule of Powers, together with the powers that a liquidator has in respect of property of a company pursuant to the *Corporations Act 2001* s 477(2).

(6) Upon completion of the realisation of property and payment of costs and expenses, and creditors, the Receiver is to deliver to:

(a) the Court; and

(b) the Commissioner of Taxation,

a statement of receipts and payments in relation to the realisation of property and payments made by the Receiver.

1. I would observe, in passing, that in cases where a liquidator of an insolvent former corporate trustee is reluctant to, or refuses to, make such an application, it would be open to the trust creditors exercising their right of subrogation to apply to the court by joining the liquidator of the insolvent former corporate trustee, for the appointment of a court appointed receiver to sell all the trust assets and distribute the proceeds (*Agusta Pty Ltd v Provident Capital Ltd* (2012) 16 BPR 30,397, per Barrett JA at [70]-[74]).
2. Of course, where a person acting as the liquidator of an insolvent former trustee company is, pursuant to the equitable lien, appointed as a court appointed receiver to sell the trust assets and, thereby, effect equitable execution, the sale is carried out by the liquidator qua court appointed receiver and not qua liquidator. The funds generated are trust funds to be used by the court appointed receiver to pay trust creditors, pursuant to the court’s directions; and the insolvent former trustee company will, thereby, be exonerated from its liabilities to those trust creditors to the extent that realised assets are able to do so.
3. I anticipate, therefore, that should the liquidator of the Company in due course apply to the Court to be appointed as the receiver to sell the remaining unsold trust property and, *nunc pro tunc* along with the former liquidators, in respect of trust property which has already been sold, it will then be open to the Court to give directions as to the manner in which the proceeds of the realised trust property are to be distributed among the trust creditors.
4. It can be seen, therefore, that vindication of the insolvent former corporate trustee’s right of indemnity through the exercise of the equitable lien, and the distribution of the proceeds of that exercise, takes place under the supervision of a court exercising power in its equitable jurisdiction.

## Question two

1. I now deal with question two.
2. As to the position in relation to the proceeds of the unfair preference claims, even though the question is certainly not free from doubt, I agree with the approach of Allsop CJ and Farrell J.
3. I now deal with the question of the distribution of the monies derived from the sale of the trust assets.
4. As mentioned, in my view, the monies held by the liquidator from the sale of the trust assets during the period January 2015 to May 2015 are the product of an unauthorised sale by the then liquidators. Therefore, on that ground alone, the statutory priority regime in s 555 and s 556 of the *Corporations Act* has no application to trust monies which the current liquidator holds from those sales.
5. However, as mentioned, there is no reason to doubt that on the application of the liquidator (together with the former liquidators), the Court would appoint them as receivers *nunc pro tunc* in respect of the sale of the trust assets which occurred in 2015. The same is true in relation to any application which the liquidator may make to the Court to be appointed receiver for the purpose of selling the remaining trust assets and distributing the proceeds to the trust creditors.
6. Therefore, in my view, the real issue which arises under this part of question two is whether it is open to this Court exercising its equitable jurisdiction in supervising the court appointed receiver’s sale of trust assets and the distribution of the proceeds thereof, to direct that in distributing the monies to the trust creditors, the receiver is to apply a regime other than pari passu.
7. In this case, the more specific question is whether the Court exercising equitable jurisdiction could direct the Court appointed receiver(s) that, in distributing the monies realised from the sale of the trust assets to trust creditors, the receiver(s) are to give a priority to employee trust creditors over trade and other trust creditors.
8. Although each case would need to be assessed according to its circumstances, for the reasons given by Allsop CJ at [111]-[120] and Farrell J at [214]-[222], I agree that this is a case where it would be open for directions to be given in the terms contemplated by Allsop CJ and Farrell J.
9. However, in my view, until the liquidator has made the application to the Court for his appointment as a receiver in respect of the sale of the unsold assets, and (along with the former liquidators) for appointment as receivers *nunc pro tunc* in respect of the assets already sold, it would not be appropriate to give the liquidator acting in his capacity as liquidator, as is the case in this application, a direction in those terms.
10. Further, I am not satisfied that it would be appropriate for the Court to give a direction preferring one group of trust creditors over another group of trust creditors, when the prospect of such a direction being made by the Court exercising equitable jurisdiction, was not squarely in issue in this application.
11. Accordingly, my answer to question two in relation to the proceeds of realisation of the trust assets is “No”. But, it is qualified because, for the reasons given, it would, in my view, be open to this Court to give a direction which gives the employee trust creditors a priority over the other trust creditors, to the liquidator, qua receiver, on the appropriate application being made.
12. There is also another basis upon which I would found the answer in [158] above. This is that, in my view, even where a liquidator of an insolvent trustee company does not have to seek equitable relief under an equitable lien to sell trust assets to vindicate the company’s right of exoneration, the statutory priority regime in s 556 of the *Corporations Act* would not apply to the payment of trust creditors from the proceeds of the sale of the trust assets. I recognise that this view may be inconsistent with *Byrnes*. However, the arguments set out below were not considered in *Byrnes* and, in my very respectful view, the arguments represent the better view.
13. In my view, it does not follow from the fact that, in *Octavo Investments Pty Limited v Knight* (1979) 144 CLR 360 and other cases, an insolvent trustee company’s right of indemnity in support of its right of exoneration, has been held to be “the property” of the company which is a proprietary interest held beneficially, that the statutory priority regime in s 556 of the *Corporations Act* applies to the assets which the insolvent company holds in its capacity as trustee upon which the right of indemnity in respect of the right of exoneration operates.
14. Section 501 of the *Corporations Act* provides as follows:

Subject to the provisions of this Act as to preferential payments, the property of a company must, on its winding up, be applied in satisfaction of its liabilities equally and, subject to that application, must, unless the company’s constitution otherwise provides, be distributed among the members according to their rights and interests in the company.

1. Section 555 of the *Corporations Act* provides as follows:

Except as otherwise provided by this Act, all debts and claims proved in a winding up rank equally and, if the property of the company is insufficient to meet them in full, they must be paid proportionately.

1. Section 556 of the *Corporations Act* relevantly provides as follows:
2. Subject to this Division, in the winding up of a company the following debts and claims must be paid in priority to all other unsecured debts and claims:

…

(e) subject to subsection (1A) — next:

(i) wages, superannuation contributions and superannuation guarantee charge payable by the company in respect of services rendered to the company by employees before the relevant date; or

(ii) liabilities to pay the amounts of estimates under Division 268 in Schedule 1 to the *Taxation Administration Act 1953* of superannuation guarantee charge mentioned in subparagraph (i);

…

(g) subject to subsection (1B) — next, all amounts due:

(i) on or before the relevant date; and

(ii) because of an industrial instrument; and

(iii) to, or in respect of, employees of the company; and

(iv) in respect of leave of absence;

1. The term “property” is defined in s 9 of the *Corporations Act* as follows:

*property* means any legal or equitable estate or interest (whether present or future and whether vested or contingent) in real or personal property of any description and includes a thing in action…

1. The definition of “property” is of a very wide ambit. On its face, the term “property of the company” in s 501 and s 555 is capable of including the company’s right of indemnity to resort to the trust assets to vindicate its right to be exonerated from a liability it has incurred in the course of carrying out its trust business.
2. A term of wide ambit should be construed in its statutory context. In *Nokes v Doncaster Amalgamated Collieries, Limited* [1940] AC 1014 (*Nokes*), the House of Lords was called on to construe the term “the property” of the company.
3. In *Nokes*, a court had made an order under s 154(1) of the Companies Act 1929 (UK) for the amalgamation of two companies which carried on the business of coal mining.
4. Section 154(1)(a) provided that the court, in ordering the amalgamation, could make an order for the transfer to the transferee company of “the property” of the transferor company. Section 154(4) then went on to provide that:

In this section the expression “property” includes property rights and powers of every description and the expression “liabilities” includes duties.

1. The question was whether a contract of employment between the transferor company and an employee was included within the definition of “the property” of the transferor company, such that on the amalgamation, the employment contract was, thereby, transferred from the transferor company to the transferee company without the consent of the employee.
2. At 1051-1052 in *Nokes*, Lord Porter observed:

Having regard to these considerations I find myself thrown back upon a consideration of the meaning to be placed on the word “property” in sub-s 1 (a). Prima facie I should not expect it to include non-transferable contracts. In truth the word “property” is not a term of art but takes its meaning from its context and from its collocation in the document or Act of Parliament in which it is found and from the mischief with which that Act or document is intended to deal. The word is used in many Acts of Parliament but I propose to confine myself to the Companies Acts themselves. The Companies (Consolidation) Act, 1908, s 122 and following sections, and the Companies Act, 1929, s 156 and following sections, deal with winding-up. Sect 151, sub-s 2, of the former Act enacts that,—

(2) The liquidator in a winding up by the Court shall have power, but (subject to the provisions of this section) in the case of a winding up in Scotland or Ireland only with the sanction of the court,—(a) to sell the real and personal property, and things in action of the company by public auction or private contract, with power to transfer the whole thereof to any person or company, or to sell the same in parcels:…(g) to do all such other things as may be necessary for winding up the affairs of the company and distributing its assets.

Sect 189 of the latter Act contains similar provisions. In neither case has it ever, so far as I know, been suggested that “property” included anything other than property of which the company then in course of being wound up could dispose.

1. In determining whether the expression the “property of the company” referred to in s 501 and s 555 of the *Corporations Act* is addressed to a company in liquidation’s right to be exonerated in respect of the liabilities incurred as trustee, the following considerations are relevant.
2. First, the underlying premise of the *Corporations Act*, as derived from its language, is that the fund to be established and distributed by the liquidator under the statutory regime of ss 501, 555 and 556, will comprise the proceeds from the realisation of property of the company which is beneficially owned by the company. This is apparent from s 501, which applies to a voluntary winding up (such as occurred in this case) and provides how “the property of the company” is to be applied. That section contemplates that the realisation of the property of the company will give rise to a fund from which, subject to the statutory regime dealing with “preferential payments”, first, the creditors will be paid, and then if there is, any surplus, it will be distributed among the members of the company. Thus, the only fund contemplated by s 501 is one in respect of which any surplus, after the payment of the creditors, is to be distributed to the “owners” of the company.
3. Importantly, s 501 does not refer to the establishment by the liquidator of any other fund to which the statutory priority regime is to apply, or at all, which is to comprise monies from the realisation of only some of the company’s property, and which is then to be used to pay only a certain category of the company’s creditors, and if there is any surplus in that fund, it is to be distributed to the beneficiaries of the trust of which the company acts, or acted, as trustee.
4. Secondly, as has been described in the reasons for judgment of Allsop CJ, a trustee’s right of exoneration is inherently incapable of generating remuneration or funds in the hands of the company which can contribute to the fund contemplated by ss 501, 555 and 556 of the *Corporations Act*. The purpose of the right of exoneration is limited to using trust assets to pay trust creditors and, to that extent, exonerate the trustee company from liability. Therefore, the right has no realisable value in the hands of the company, and the exhaustion of the exercise of the right of exoneration by the company as an incident of the office of trustee, is incapable of contributing monies to the fund of monies to be distributed to the creditors of the company in accordance with the statutory regime in s 556 of the *Corporations Act*.
5. There is also a very significant aspect of the right of indemnity of an insolvent trustee company which illustrates the lack of the realisable value of that right of indemnity and exoneration in the hands of the company. This is that a company’s right of indemnity in respect of the right of exoneration and the attendant equitable lien, is by the time of the appointment of a liquidator to the company subrogated to the unpaid trust creditors. Like Farrell J, I do not accept the argument that this right of subrogation has been abrogated by s 500(2) of the *Corporations Act*. To effect such a significant infringement upon common law rights would require explicit language.
6. As persons to whom the rights of indemnity and the attendant equitable lien have been subrogated, the trust creditors of an insolvent corporate trustee, if so minded, are able to exercise the trustee’s rights directly over the trust property. As mentioned above, this can occur by the creditors, in an application to which the liquidator is joined as a party, applying for a judicial sale of the trust assets, or for appointment of a receiver to undertake the sale of the trust assets and to distribute the proceeds among the trust creditors.
7. The proposition that property of the company which has no realisable value in the hands of the company on insolvency, does not form part of the assets of the company which may become available to creditors is supported by Professor Goode in *Principles of Corporate Insolvency Law* (4th ed, Sweet & Maxwell, 2011) p 187, who states:

A right which, although in itself transferable, is inseparably annexed to personal status and cannot be transferred so as to produce value for the company, is not a free‑standing asset that can be treated as part of the company’s estate. It is necessary to emphasise that what we are concerned with is not whether an asset is capable of transfer by the company, but whether it is transferable so as to produce value for the company.

1. Further, the assets held by a company on trust before the company goes into liquidation are not assets available for sale by the company to generate funds for the trustee company’s own benefit. As *In re Suco Gold Pty Ltd (In Liq)* (1983) 33 SASR 99 (*Suco Gold*) has held, the character of those assets as trust assets does not change after the company goes into liquidation.
2. Thirdly, it is a fundamental principle that the liquidator when appointed to a company takes the company’s property as he finds it. This is true of the right of indemnity in support of the right of exoneration of the trustee company.
3. The High Court made the following observations as to the nature of the right of exoneration inherited on the liquidation of a trustee company in *Chief Commissioner of Stamp Duties (NSW) v Buckle* (1998) 192 CLR 226 at 247 (*Buckle*):

A court of equity may authorise the sale of assets held by the trustee so as to satisfy the right to reimbursement or exoneration. In that sense, there is an equitable charge over the “trust assets” which may be enforced in the same way as any other equitable charge. *However, the enforcement of the charge is an exercise of the prior rights conferred upon the trustee as a necessary incident of the office of trustee.* It is not a security interest or right which has been created, whether consensually or by operation of law, over the interests of the beneficiaries so as to encumber them in the sense required by s 66(1) of the Act.

(Footnote omitted. Emphasis added.)

1. It is significant that the right has been described by the High Court in *Buckle* as an element of the prior rights conferred upon the trustee as a necessary incident of the office of trustee. Further, it is apparent from the observations in *Buckle* that the exercise of that right and the attendant equitable lien, as a means of the vindication of the right of exoneration is regulated by equitable principles. Thus, when, after liquidation, the liquidator exercises the inherited right, it is the exercise of a right which accrued prior to the liquidator’s appointment, and which is attended by the same trust and equitable properties as attended that right prior to the appointment. In other words, the vindication of the right of exoneration by a trustee, whether solvent or insolvent, is the operation of a “necessary incident of the office of trustee” and is effected under the laws of trust and equity.
2. This analysis is consistent with the approach of Needham J in the case of *Re Staff Benefits Pty Ltd* [1979] 1 NSWLR 207 (*Staff Benefits*). That was not a case involving a company in liquidation which had been removed as trustee of a trust and was, therefore, a bare trustee. Needham J considered whether the statutory priority regime comprised in s 291 of the *Companies Act 1961* applied to the distribution of trust monies the subject of the trustee’s right of exoneration and equitable lien. Needham J found that the distribution of the trust monies to the trust creditors by the insolvent trustee company in the exercise of the right of exoneration, took place under the principles of the common law, namely, as he put it, “the principle of indemnity and lien”.
3. In that case, a company, Staff Benefits Pty Ltd, acted as trustee of a general investment fund. The beneficiaries of the fund were the investors in the fund. In the course of carrying out its duties as trustee for the fund, the company accepted monetary deposits from depositors.
4. The company went into liquidation. There was a contest between the creditors of the trustee company, being the depositors, on the one hand; and the beneficiaries of the trust, being the investors whose funds comprised the trust funds, on the other hand.
5. The liquidator of the company applied for directions as to how to deal with the claims by the creditors and by the investors.
6. Needham J held that the trustee had a right of indemnity in respect of the claims made by the depositors and that the depositors were entitled to be subrogated to that right of indemnity. Accordingly, Needham J found that the priority was with the depositors and not the investors.
7. There was then a question as to whether the appropriate interest rate to be applied to the monies due to the depositors was the interest rate provided for under the statutory regime for the winding up of insolvent companies, or not. Needham J found that the interest rate under the statutory winding up regime did not apply because the trust funds in respect of which the trustee’s right of indemnity had operated, were not assets of the company for the purposes of s 291 of the *Companies Act*. Relevantly, Needham J observed at 215:

The claim of the depositors against the company is for the amount of their debts. In a situation where the funds available are not sufficient to meet the claims of the investors and of the depositors, it must be the case that payment of the claims of the depositors in full involves making an inroad into funds which would otherwise be held in trust for the investors. *Those funds are not “assets of the company”*, *and the justification for preferment of the depositors is not any rule of bankruptcy administration, but the principle of indemnity and lien earlier discussed.*

(Emphasis added.)

1. It is apparent that Needham J considered thatthe process of exoneration, whereby the trust assets were used to pay the trust creditors, occurred by reference to common law principles, and dehors the statutory priority regime provided for in s 291 of the *Companies Act*. I observe, in passing, that *Staff Benefits* was not addressed by the South Australian Full Court in *Suco Gold*.
2. As mentioned, the exoneration process which is effected under equitable principles, results in the payment of trust creditors from the trust assets, but that process does not yield any funds to the company in liquidation capable of contributing to the fund contemplated by ss 501, 555 and 556 of the *Corporations Act*. In other words, the “property of the company” referred to in s 501 and s 555, is, in my view, addressed to the property of the company capable of producing monies to contribute to the fund contemplated in ss 501, 555 and 556. It does not include rights which have no realisable value in the hands of the company.
3. To the extent that the trust creditors’ debts are not satisfied by the exercise by the company, as an incident of its office of trustee, of its right of exoneration, the trustee creditors will be entitled to prove, along with any other creditors, whether general or otherwise, of the company in the winding up of the company and the statutory winding up regime including s 556 will apply to those proofs of debt.
4. It follows, in my very respectful view, that the better view is that on a proper construction of the *Corporations Act*, the words “property of the company” in s 501 and s 555 of the *Corporations Act* are not addressed to a trustee company’s right of indemnity.

## Question three

1. I would for the reasons given above, answer question three in the positive as to the unfair preference proceeds and in the negative for the proceeds of the realisation of trust assets.

## Question four

1. For the reasons given above, namely, that any distribution of the proceeds of the realisation of the trust assets should be made by a court approved receiver, and that such distribution may be other than pari passu, I would answer question four in the negative.

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| I certify that the preceding seventy‑two (72) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Siopis. |

Associate

Dated: 21 March 2018

REASONS FOR JUDGMENT

FARRELL J:

1. I have had the benefit of reading the reasons for decision of both Allsop CJ and Siopis J. As noted by Allsop CJ, delivery of our judgments in this matter was imminent at the time the Victorian Court of Appeal delivered its judgment in *Commonwealth v Byrnes**and Hewitt* *in their capacity as joint and several receivers and managers of Amerind Pty Ltd (Receivers and Managers appointed) (in liquidation)* [2018] VSCA 41 (***Amerind****)*. My judgment has been altered as necessary to take account of that decision.
2. I will adopt the format of Allsop CJ’s reasons and the fundamental proposition that in answering the questions posed by the parties against the factual background of this case, the reasoning used to answer those questions must recognise the wider and different circumstances that may arise in other insolvencies.

## Applicable General Principles

1. Respectfully, I agree with the Chief Justice’s analysis of the relevant case law and principle under this heading.
2. Specifically, I agree with the conclusions reached at [78]-[79] and the passage of the judgment of King CJ from ***In re Suco Gold*** *Pty Ltd (in liq)* (1983) 33 SASR 99 quoted at [76] of the Chief Justice’s reasons. Having regard to the intrinsic nature of a trustee’s right of indemnity through exoneration from trust assets and the lien over those assets for that purpose amounting to a proprietary interest which has priority to the interests of beneficiaries, trust assets are available to pay trust creditors but not to pay other creditors of an insolvent corporate trustee. I therefore also agree with Allsop CJ’s conclusion stated at [4] and [30] of his reasons that *In re Suco Gold* is correct and that ***Re Enhill*** *Pty Ltd* [1983] 1 VR 561 is wrongly decided in relation to the availability of trust assets to pay creditors of the insolvent corporate trustee who are not trust creditors. I also agree with [81]-[82] of the Chief Justice’s reasons.

## Question 1: Did the liquidator have power to sell the trust assets by reference to the power in s 477 of the *Corporations Act*?

1. I agree with the Chief Justice’s response to this question for the reasons that he gave: see [85]-[92]. I agree with Allsop CJ and Siopis J that in the circumstances of this case, Martin Bruce Jones has no apparent conflict of interest which would disqualify him from being appointed as a receiver for the purpose of selling trust assets. I therefore agree with Siopis J at [140] that upon application by Mr Jones (and any other joint liquidators in office at the time of the sales), it would be appropriate for such an order to be made *nunc pro tunc* to authorise sales of assets which have already occurred and to appoint Mr Jones as receiver in relation to sales of assets yet to occur. Such orders would be made by a Judge of this Court sitting as a court of Equity. I will address how the proceeds of the sales might be dealt with in response to question 2.

## Question 2: Are either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds to be applied by the Plaintiff in accordance with the priority regime established by sections 555, 556, 560 and 561 of the *Corporations Act*?

1. Although I consider that the parties’ position on the issue of how the Unfair Preference Proceeds should be applied is open to question, I agree with the Chief Justice’s response to the approach that this bench should adopt for the reasons which he gave at [93]-[94].
2. I accept that the Victorian Court of Appeal’s decision in *Amerind* is binding on this bench (which is not exercising appellate jurisdiction) and supports Allsop CJ’s conclusions at [101]-[102]. This is despite the factually different circumstances of the case under consideration in *Amerind* and this case, in which the trustee lost office upon the appointment of the liquidator. For that reason, I will adopt the Chief Justice’s answer to Question 2 “Yes as to both” in the circumstances of this case.
3. I note that although I would not have taken the same path to that result, I have come to the conclusion that in this case a court of Equity should authorise the distribution of trust assets in paying the reasonable remuneration and costs of the liquidator (including costs incurred as receiver) in the priority provided by s 556(1) of the *Corporations Act 2001* (Cth)(following the principles summarised in *Re AAA Financial Intelligence Ltd (in liq)* [2014] NSWSC 1004 at [13] per Brereton J) and employee related expenses in the order set out in ss 556(1)(e), (f), (g) and (h). That is because of the breadth of the trustee’s authority and the indemnity under the trust deed in this case. I can envisage circumstances where the trustee’s indemnity might not cover some liabilities (for instance, for fines or penalties related to late payments) under the terms of the trust deed, where payments out of trust assets could not be made. Although it is not relevant in this case (because it is a voluntary liquidation), I do not accept that the costs of an application to wind up the corporate trustee constitutes a trust debt. I agree with Allsop CJ that each paragraph of s 556 must be interrogated for its meaning.
4. Set out below is the reasoning which brought me to the conclusions in the immediately preceding paragraph.
5. The question of whether the proceeds of realisation of trust assets should be applied in accordance with the **priority regime** established by ss 555, 556, 560 and 561 (and their statutory predecessors) has been the subject of significant academic debate and conflicting decisions of Courts for the better part of fifty years. The priority regime and the definition of “property” in s 9 of the *Corporations Act* are generalised. While that may be appropriate for guiding the distribution of assets of an insolvent company which has only ever conducted business in its own right, it has proved inadequate to provide sufficient certainty in relation to the resolution of issues which arise upon the insolvency of a corporate trustee which has operated one or more trading trusts.
6. As observed by Dr Nuncio D’Angelo and many other commentators, the trust form has proved to be a flexible – and often tax effective – platform for investment in a range of assets, particularly in family run businesses and large scale infrastructure projects.
7. The statistics quoted by Dr D’Angelo in his paper “Commercial trusts in practice: the trust as a surrogate company” presented at the Annual Commercial and Corporate Law Conference convened in November 2016 by the Supreme Court of New South Wales demonstrate the important role that trading trusts now play in Australia’s economic life. At pages 10-11, Dr D’Angelo notes that, while statistics are naturally thin (since many trusts have no obligation to report publicly), the Australian Securities and Investments Commission said that as at June 2015, there were 3,600 managed investment schemes. Based on information from the Australian Taxation Office for the fiscal year to June 2014, there were more tax returns lodged in respect of trusts than either of companies or partnerships in that year: there were 802,000 tax returns for trusts declaring total income of $345 billion; 763,000 tax returns for companies declaring income of $2.7 trillion; and 344,000 tax returns for partnerships declaring income of $148 billion.
8. The issues which arise in the application of the generalised priority regime (under statutory predecessors of the *Corporations Act*)to insolvent corporate trustees of trading trusts have been the subject of comment since the late 1970s, with conflicting commentary by leading academics and judges. The issues and possible solutions were clearly addressed in the Australian Law Reform Commission’s Report 45 “General Insolvency Inquiry” based on the law as it existed in September 1988. Since then, a further complicating factor has been legislation enacted by the Commonwealth Government designed to protect the interests of employees, such as the *Fair Entitlements Guarantee Act 2012* (Cth) and the legislation relating to payment of superannuation guarantee charges considered by Brereton J in *Re Independent Contractor Services (Aust) Pty Ltd ACN 119 186 971 (in liq) (No 2)* [2016] NSWSC 106; 305 FLR 222.
9. In my view it is unfortunate that the legislature has not seen fit to make more explicit the extent to which the priority regime set out in the *Corporations Act* impacts on the interests of those involved with a trading trust where a current or former trustee is a company in liquidation. There are good public policy reasons for a legislated priority regime which expressly encompasses an insolvent corporate trustee given the position that such trusts occupy in Australia’s economy. Some of the economic justifications for establishing unambiguous regimes for priorities in insolvent administrations are so that assets may be efficiently deployed in the economy (rather than locked up during protracted insolvent administrations) and so that returns to creditors, investors and beneficiaries are maximised rather than monies being expended on applications to the courts for directions in order to provide certainty and protect the position of liquidators.
10. I acknowledge that the task of amending the priorities regime in the *Corporations Act* to address these issues would not be straightforward. However, it would be appropriate for the legislature to make clear whether it prefers the policy approach reflected in the decisions in *Re Enhill*, *In re Suco Gold* or *Re Independent Contractors* or some other approach. Honest minds can differ about which approach is preferable, even in the relatively straightforward case of a trading trust carrying on only one family business. The Victorian Court of Appeal did not attempt to resolve the question of whether the approach in *Re Enhill* or *In re Suco Gold* was to be preferred. This bench prefers the approach in *In re Suco Gold* because it is more consistent with principle and better accommodates more complex situations.
11. It would be important that any re-drafting of the priority regime accommodates the more complex situations of a trustee of multiple funds or where the trustee also conducts business in its own right. In the more complex situations, trusts are a vehicle for investments from the Australian public, often in the context of superannuation savings, where many funds may be involved and the interests of diverse beneficiaries and creditors will need protection. This is a matter of important public policy, given the benefits of relative certainty referred to above, Australia’s adoption of a policy of compulsory superannuation savings and the proliferation of trusts which operate businesses. Having said that, not all drafting tasks would be difficult: for instance, to make it clear whether trust assets can be used to pay the costs of the application to wind up the trustee company.
12. Turning to the application under consideration, it is undoubtedly the case that the right of exoneration and the lien which attaches to trust property for the purposes of its protection and enforcement is “property” for the purposes of s 9 of the *Corporations Act*. In my view, King CJ was clearly right in *In re Suco Gold* when he said, at 33 SASR 99 at 108 (footnotes omitted):

If the trust liabilities have been discharged, the trustee in bankruptcy or liquidator is entitled to recoup the bankrupt estate out of the trust property and the proceeds of the right of indemnity become part of the property divisible among the creditors. If the liabilities have not been discharged, the trustee in bankruptcy or liquidator may, by reason of the right of indemnity which vests in him, apply the trust property to the payment of the trust liabilities, thereby exonerating the bankrupt estate to the extent of the value of the available trust assets. In the latter circumstances there cannot be proceeds of the right of indemnity which are available for distribution among the general body of creditors.

1. This is consistent with the judgment of Allsop CJ at [59]-[69] which to my mind correctly summarises the law having regard to the High Court’s decisions in ***Octavo Investments*** *Pty Ltd v Knight* [1979] HCA 61; 144 CLR 360 at 367-370, *Chief Commissioner of Stamp Duties (NSW) v Buckle* [1998] HCA 4; 192 CLR 226 and *Bruton Holdings Pty Ltd (in liq) v Commissioner for Taxation* [2009] HCA 32; 239 CLR 346. I would emphasise Allsop CJ’s conclusion at [69]: trust assets are not property of the company, but the trustee’s right of exoneration supported by the lien in the character of a proprietary interest is. It is, however, property of a particular character, with its content and shape determined by the purpose for which it came into existence – the payment of creditors the liability to whom was incurred in executing the trust. The reasoning of Derrington J in *Lane (Trustee), in the matter of Lee (Bankrupt) v Deputy Commissioner for Taxation* [2017] FCA 953 is consistent with this reasoning. I prefer Derrington J’s approach to that adopted by the Victorian Court of Appeal in *Amerind* at [274]-[281]. Nothing turns on the fact that the word “proceeds” is not used in the relevant provisions of the *Corporations Act*; the reasoning is about the nature of the trustee’s right of exoneration and the creditor’s right of subrogation. In my view, the exercise of the right of exoneration is incapable (of its nature) of producing “proceeds”: it is the act of payment to trust creditors from trust assets which produces the exoneration and that is the reason why trust assets are not available to creditors who are not trust creditors. This is what gives effect to the trust creditors’ right to be subrogated to the trustee’s right of indemnity.
2. Further, while payment out of the trust assets relieves the trustee’s estate of personal liability and exhausts the lien, it need not be the case that that payment will be made by the trustee for distribution under the priority regime. By subrogation, trust creditors have a right to call for the administration of the trust and payment out of the trust fund. (I do not accept submissions that the mere existence of s 500(2) of the *Corporations Act* destroys the rights of subrogation expressly referred to in *Octavo* *Investments* by requiring that a creditor obtain the leave of the Court before joining the former trustee company to such a claim.) In this case, the Company ceased to be trustee of the trust upon the appointment of a liquidator and the Company lost its right to sell trust assets. Had the liquidators taken the appropriate course, the Court would have appointed the liquidator or someone else as receiver for the purpose of selling the trust assets and the Court would have made directions for the remuneration of the receiver followed by directions as to payment of trust assets to the trust creditors. Acting as a court of Equity, the Court would have then had to decide in what order trust creditors should be paid. The trustee’s proprietary interest must be recognised, but that is done by ensuring that only trust creditors are paid. By payment in accordance with the Court’s directions, the receiver or liquidator does not dispose of “property of the company” but trust assets.
3. I have previously not been satisfied that it follows from King CJ’s reasoning set out above that the priority regime (as then drafted) should be applied to the payment of trust creditors. In *Woodgate, in the matter of Bell Hire Services**Pty Ltd (in liq)* [2016] FCA 1583, I accepted that trust creditors ranked *pari passu* for the payment of trust debts out of trust assets. That view was consistent with the views of the learned authors of *Jacobs’ Law of Trusts in Australia* (8th ed, LexisNexis Butterworths, 2016), the Honourable JD Heydon and Justice MJ Leeming of the Court of Appeal of New South Wales, at [21-15] and views expressed by Brereton J in *Re Independent Contractor Services (Aus) Pty Limited ACN 119 186 971 (in liq) (No 2)* [2016] NSWSC 106; 305 FLR 222.
4. However, having regard to submissions made in this case, I have now come to the view that a court of Equity should follow the statute in giving a receiver (or liquidator acting as receiver) directions as to how trust creditors (and only trust creditors) should be paid out of trust assets. There are many reasons for this.
5. First, the order in which payment must be made in such cases cannot be regarded as settled: see *Jacobs’ Law of Trusts* at [21-15].
6. Second, it is true that in most cases, “equality is equity” is the appropriate guiding precept. That is also the guiding principle under the winding up provisions of the *Corporations Act*. While s 556 (and its statutory predecessors) creates priority among unsecured creditors, it is a relatively limited regime through which the legislature has sought to accommodate particular interests or values. The preferred position of the liquidator reflects the need to ensure that there will be professionals willing to provide this service; the same rationale is applied to the priority afforded by courts to the remuneration of court appointed receivers. The preferred position accorded to employees over other unsecured creditors and some secured creditors under the *Corporations Act* and the introduction of the *Fair Entitlements Guarantee Act* reflect a long held position of legislatures in the United Kingdom and Australia that it works undue hardship on employees to fail to afford them some priority in the insolvent administration of companies.
7. The priority accorded to the liquidator and employees in legislation regulating the winding up of corporations is of long standing. In Chapter 2 of Symes CF, *Statutory Priorities in Corporate Insolvency Law* (Ashgate Publishing Limited, 2008), the author usefully traces the evolution of statutory priorities in the United Kingdom and Australia from the basal position of payment of creditors *pari passu*. Until well into the twentieth century, the legislation regulating the incorporation and winding up of companies enacted by Australian States largely followed the pattern of the United Kingdom’s law with respect to winding up.
8. As noted in *Amerind* at [220],priority was first given to wages and salaries of employees in bankruptcy legislation in the United Kingdom in 1825.While the *Companies Act 1862* (UK) had some provisions dealing with winding up it did not afford priority to employees’ wages. British Parliamentary debates of the 1880s and 1890s concerned whether workers’ wages should be afforded priority where the company in winding up is insolvent. Debate on the *Preferential Payments in Bankruptcy Bill 1888* (UK) focussed on the vulnerable position of servants and labourers. The issue was revisited in 1897 in relation to whether such people should also have priority over charge holders. In *Statutory Priorities in Corporate Insolvency Law* at pages 29-30, the author quotes from the debates in relation to the *Preferential Payments in Bankruptcy Amendment Act 1897* (UK). One example is as follows (footnotes omitted):

The Hon J.A.Mundella … said that a ‘workmen ought to have prior claim over all others on the ground first, that the workmen had not the means, and it was not their business, to inquire into the solvency of the parties for whom they worked’. He noted that the position of the worker differed from that of the ordinary creditor, who inquired into the solvency of the people they were dealing with and took risk with the rest of the creditors. In a justification that could have been submitted in more recent litigation, Mundella argued for wages’ priority ‘because every stroke of work the workmen did to the last moment of his employment contributed to increase the value of the assets for all the creditors’.

…

In summing up the debate, the Solicitor General observed that ‘in every part of the House [there was] a general agreement as to the fairness of the principle on which the Bill was founded’.

1. Although the language used in the debates is dated, it accurately reflects the requirements of fairness (on which equitable principles are based) to address vulnerability of employees in relation to the insolvency of companies which employ them.
2. In 1893 the Western Australian parliament passed the *Companies Act 1893* (WA). Sections 154, 155 and 163 contained the following provisions with respect to priorities. They reflect the position in the United Kingdom before the passage of the amending bill in 1897:

*Provisions applying to Winding-up, whether under the Order of
the Court or Voluntary.*

…

154. (1) IN the distribution of the assets of any company being wound up there shall be paid in priority to all other debts:

(a) All wages or salary of any clerk or servant in respect of services rendered to the company during four-months before the date of the commencement of the winding up, not exceeding Fifty pounds; and

(b) All wages of any labourer or workmen, not exceeding Twenty-five pounds, whether payable for time or for piecework, in respect of services rendered to the company during two months before the commencement of the winding up: Provided that where any labourer in husbandry has entered into a contract for the payment of a portion of his wages in a lump sum at the end of the year of hiring, he shall have priority in respect of the whole of such sum, or a part thereof, as the Court may decide to be due under the contract, proportionate to the time of service up to the commencement of the winding up.

(2) The above-mentioned debts shall rank equally between themselves and shall be paid in full, unless the assets of the company are insufficient to meet them, in which case they shall abate in equal proportions between themselves.

(3) Subject to the retention of such sums as may be necessary for the costs of the winding up or otherwise, the above-mentioned debts shall be discharged forthwith, so far as the assets of the company are sufficient.

155. THE property of the company shall, subject to the provisions of the last preceding section be applied in satisfaction of its liabilities *pari passu*, and subject thereto shall, unless it be otherwise provided by the articles, be distributed amongst the members according to their rights and interests in the company.

…

163. ALL costs, charges and expenses properly incurred in the winding up of the company, including the remuneration of the liquidator, shall be payable out of the assets of the company, in priority to all other claims.

1. Since that time, the priority position of employees in legislation dealing with the winding up of companies has only been enhanced and the position of liquidators for their reasonable remuneration, costs and expenses has been preserved.
2. Third, the cardinal principle of equity is that the remedy must be fashioned to fit the nature of the case and particular facts: see *Bofinger v Kingsway Group Limited* [2009] HCA 44; 239 CLR 269 at [1] per the Court. Where, as here, a company in liquidation has been formed to operate as trustee of a trading trust to conduct a business which could (but for access to the capacity to income split or other taxation advantages) have equally plausibly have been conducted by the Company in its own right, it is difficult to see why the same order of priority as prescribed in the priority regime under the *Corporations Act* should not be accorded to liquidators and employees (and those who stand in the employees’ shoes having paid some measure of the employees’ entitlements to them) under equitable principles.
3. In summary, even if I did not feel bound to follow the decision in *Amerind* on this issue, in this case, equity should follow the statute in the order of payment of liabilities to trust creditors properly in exercise of the right of exoneration. I agree with Allsop CJ that each paragraph of s 556 must be considered individually in light of the nature of the right of exoneration; it cannot be assumed that that right will provide access to trust assets under each paragraph. I have formed my opinion in light of the prevalence of trading trusts, the legislative focus on protecting employee entitlements for over a century and the fact that equitable remedies should be shaped to fit the circumstances.

## Questions 3: Should the Plaintiff be directed under s 511 of the Act to deal with either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds as assets in the winding up of the Company?

1. The answer to question 3 should be that directions should be given in accordance with the answer to question 2.

## Question 4: Alternatively, should the Plaintiff be directed under s 511 of the Act that either or both the proceeds of realisation of the Trust Assets and the Unfair Preference Proceeds be distributed by the Plaintiff to unsecured creditors of the Trust pari passu after providing for the costs of administration (including the Administrators’ and Liquidators’ remuneration and expenses) only?

1. For reasons given above, the answer to question 4 is “no”.

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| I certify that the preceding thirty-two (32) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Farrell. |

Associate:

Dated: 21 March 2018