FEDERAL COURT OF AUSTRALIA

Hussain v CSR Building Products Limited, in the matter of FPJ Group Pty Ltd (In Liq) [2016] FCA 392

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| File number: | QUD 153 of 2015 |
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| Judge: | **EDELMAN J** |
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| Date of judgment: | 13 May 2016 |
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| Catchwords: | **CORPORATIONS** – claim to recover alleged unfair preferences under s 558FE of the *Corporations Act –* whether company insolvent at the time of making payments – whether payments were in relation to “unsecured debts” – meaning of an “unsecured debt” in s 588FA(1)(b) – whether a retention of title clause is a “security” – date for determination of the value of security in s 588FA(2) – operation of “good faith” in s 588FG(2) – operation of “suspicion” in s 588FG(2) – whether running account existed – whether defendant has a set-off under s 553C – whether set-off under s 553C can be made against a preference claim under s 588FF |
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| Legislation: | *Bankruptcy Act 1966* (Cth) s 122  *Chattel Securities Act 1987* (Vic) s 3(1)  *Corporations Act 2001* (Cth) Part 5.7B; ss 9, 51, 51A, 51E, 95A(1), 95A(2), 442CC, 442CC(2), 442CB, 553C, 553C(1)(a), 553C(2), 588E(3)(b), 588F, 588FA, 588FA(1), 588FA(1)(b), 588FA(2), 588FA(3), 588FC, 588FE, 588FF, 588FF(1)(c), 588FG(1)(a), 588FG(2), 588FG(2)(a), 588FG(2)(b), 588FG(2)(b)(i), 588FG(2)(b)(ii), 588V, 588W  *Personal Property Securities Act 2009* (Cth) ss 12(1), 12(2)(d), 306(2)(b), 307, 308(a), 310, 310(d), 322(1)  *Personal Property Securities (Corporations And Other Amendments) Bill 2010* (Cth) |
|  |  |
| Cases cited: | *Airservices Australia v Ferrier* [1996] HCA 54; (1996) 185 CLR 483  *Aluminium Industrie Vaassen BV v Rompala Aluminium Ltd* [1976] 2 All ER 552  *Associated Alloys Pty Ltd v Metropolitan Engineering & Fabrication Pty Ltd (Voluntary Administrators Appointed) (Receivers and Managers Appointed)* (1998) 16 ACLC 1633  *Associated Alloys v ACN 001 452 106 Pty Ltd (in liq)* [2000] HCA 25; (2000) 202 CLR 588  *Australian Securities & Investments Commission v Plymin* [2003] VSC 123; (2003) 175 FLR 124  *Baden v Société Générale pour Favoriser le Dévelopment du Commerce et de l’Industrie en France SA* [1992] 4 All ER 161  *Bank of Australasia v Hall* [1907] HCA 78; (1907) 4 CLR 1514  *BP Australia Ltd v Brown* [2003] NSWCA 216; (2003) 58 NSWLR 322  *Burness, In the matter of Denward Lane Pty Ltd (ACN 065 418 411) (In Liquidation)* [2009] FCA 893  *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd* [2011] NSWCA 109; (2011) 81 NSWLR 47  *Carello as Liquidator of Perrinepod Pty Ltd (In Liq) v Perrine Architecture Pty Ltd* [2016] WASC 145  *Cashflow Finance Pty Ltd (in liq) v Westpac Banking Corp* [1999] NSWSC 671  *Central Cleaning Supplies (Australia) Pty Ltd v Elkerton* *(in his capacity as joint and several liquidator of Swan Services Pty Ltd (in liq))* [2015] VSCA 92; (2015) 321 ALR 181  *Clifton v CSR Building Products Pty Ltd* [2011] SASC 103  *Craine v Colonial Mutual Fire Insurance Co Ltd* [1920] HCA 64; (1920) 28 CLR 305  *Cussen (as Liquidator of Akai Pty Ltd) v Commissioner of Taxation* [2004] NSWCA 383; (2004) 51 ACSR 530  *Cussen v Sultan* [2009] NSWSC 1114; (2009) 74 ACSR 496  *Davies v Chicago Boot Co Pty Ltd* [2011] SASC 27  *Dean-Willcocks v Commissioner of Taxation* [2008] NSWSC 1113  *Duncan v Commissioner of Taxation; in the matter of Trader Systems International Pty Ltd (in liq)* [2006] FCA 885  *Expense Reduction Analysts Group Pty Ltd v Armstrong Strategic Management and Marketing Pty Limited* [2013] HCA 46; (2013) 250 CLR 303  *Expo International Pty Ltd v Chant* [1979] 2 NSWLR 820  *Farah Constructions Pty Ltd v Say–Dee Pty Ltd* [2007] HCA 22; (2007) 230 CLR 89  *Foots v Southern Cross Mine Management Pty Ltd* [2007] HCA 56; (2007) 234 CLR 54  *Fortress Credit Corporation (Australia) II Pty Ltd* [2015] HCA 10; (2015) 254 CLR 489  *General Motors Acceptance Corp Australia v Southbank Traders Pty Ltd* [2007] HCA 19; (2007) 227 CLR 305  *Globe Motors, Inc v TRW Lucas Varity Electric Steering Ltd* [2016] EWCA Civ 396  *Hall v Poolman* [2007] NSWSC 1330; (2007) 65 ACSR 123  *Hamilton v BHP Steel (JLA) Ltd* (1995) 13 ACLC 1  *In re Nortel GmbH (in administration) and related companies* [2013] UKSC 52;[2014] AC 209  *Jetaway Logistics Pty Ltd v Deputy Commissioner of Taxation* [2009] VSCA 319; (2009) 26 VR 657  *JLF Bakeries Pty Ltd (in liq) v Baker’s Delight Holdings Ltd* [2007] NSWSC 894; (2007) 64 ACSR 633  *Kazar v Kargarian* [2010] FCA 1381; (2010) 81 ACSR 158  *Lee Kong v Pilkington (Australia) Ltd* (1997) 25 ACSR 103  *Lewis, in the matter of Damilock Pty Ltd (In Liquidation) ACN 008 083 985 v VI SA Australia Pty Ltd ACN 002 433 267* [2008] FCA 1801  *Lopez (In his capacity as liquidator of Swan Concrete Products Pty Ltd (in liq)) v Harvey* [2015] WASC 292  *Manpac Industries Pty Ltd v Ceccattini* [2002] NSWSC 330; (2002) 20 ACLC 1,304  *Matthews v The Tap Inn* [2015] SADC 108  *Mineralogy Pty Ltd v Sino Iron (No 6)* [2015] FCA 825  *New Cap Reinsurance Corporation Ltd v A E Grant* [2009] NSWSC 662; (2009) 72 ACSR 638  *Olifent v Australian Wine Industries Pty Ltd* (1996) 19 ACSR 285  *Queensland Bacon Pty Ltd v Rees* [1966] HCA 21; (1966) 115 CLR 266  *Re Bird; Ex parte M & G Casabene & Sons* (1979) 39 FLR 281  *Re Emanuel (No 14) Pty Ltd (in liq); Macks v Blacklaw & Shadforth Pty Ltd* (1997) 147 ALR 281  *Re Parker* (1997) 80 FCR 1  *Re Toowong Trading Pty Ltd (In Liq)* [1989] 1 Qd R 207  *Re Tweed Garages Ltd* [1962] Ch 406  *Rees v Bank of New South Wales* [1964] HCA 47; (1964) 111 CLR 210  *Roberts v Investwell Pty Ltd (in liq)* [2012] NSWCA 134; (2012) 88 ACSR 689  *Sandell v Porter* [1966] HCA 28; (1966) 115 CLR 666  *Sheahan Pty Ltd v Murdock & Gediz Pty Ltd* [2008] SADC 5  *Sheahan v Fabienne Pty Ltd* [1999] SASC 335  *Shirlaw v Lewis* (1993) 10 ACSR 288  *Singer v Williams* [1921] 1 AC 41  *Smith v Boné in the matter of ACN 002 864 002 Pty Ltd (in liq)* [2015] FCA 319  *Southern Cross Interiors Pty Ltd (In Liq) v Deputy Commissioner of Taxation* (2001) 53 NSWLR 213  *Standard Chartered Bank of Australia Ltd v Antico (Nos 1 & 2)* (1995) 38 NSWLR 290  *Sutherland v Liquor Administration Board* (1997) 15 ACLC 875  *Sutherland v Lofthouse* [2007] VSCA 197; (2007) 214 FLR 157  *Sydney Appliances Pty Ltd (in liq) v Eurolinx Pty Ltd* [2001] NSWSC 230  *The Tap Inn Pty Ltd v Matthews* [2015] SASCFC 188  *VR Dye & Co v Peninsula Hotels Pty Ltd (in liq)* [1993] 3 VR 201  *Walsh v Natra Pty Ltd* [2000] VSCA 60  *Williams (as liquidator of Scholz Motor Group P/L (in liq)) v Peters* [2009] QCA 180; (2009) 232 FLR 98  *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1989] EWCA Civ 5; [1990] 1 All ER 512  Commonwealth, *Parliamentary Debates*, House of Representatives, 10 March 2010, 2009 (Dr Craig Emerson)  Bant E, *The Change of Position Defence* (Hart Publishing, 2009)  Derham R, *Derham on the Law of Set-off* (4th ed, Oxford University Press, 2010)  Derham R, “Set-off Against Statutory Avoidance and Insolvent Trading Claims in Company Liquidation” (2015) 89 *Australian Law Journal* 459 |
|  |  |
| Date of hearing: | 19-20, 22 April 2016 |
|  |  |
| Registry: | Queensland |
|  |  |
| Division: | General Division |
|  |  |
| National Practice Area: | Commercial and Corporations |
|  |  |
| Sub-area: | Corporations and Corporate Insolvency |
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| Category: | Catchwords |
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| Counsel for the Plaintiffs: | Mr V Brennan |
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| Solicitor for the Plaintiffs: | Taylor David Lawyers |
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| Counsel for the Defendant: | Mr R Schulte |
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| Solicitor for the Defendant: | Scoglio Law |

ORDERS

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|  | | QUD 153 of 2015 |
| IN THE MATTER OF FPJ GROUP PTY LTD (IN LIQUIDATION) ACN 146 152 561 | | |
| BETWEEN: | SHAHIN HUSSAIN AND DAVID ROSS AS JOINT AND SEVERAL LIQUIDATORS OF FPJ GROUP PTY LTD (IN LIQUIDATION) ACN 146 152 561  Plaintiffs | |
| AND: | CSR BUILDING PRODUCTS LIMITED ACN 008 631 356  Defendant | |

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| --- | --- |
| JUDGE: | EDELMAN J |
| DATE OF ORDER: | 13 MAY 2016 |

THE COURT ORDERS THAT:

1. The application be dismissed.

2. The plaintiffs pay the defendant’s costs to be taxed if not agreed.

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

REASONS FOR JUDGMENT

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EDELMAN J:

## Introduction

1 This litigation was unfortunate and uncommercial. It involved a claim by the liquidators of FPJ Group Pty Ltd **(FPJ Group**) to recover payments from CSR Building Products Pty Ltd (**CSR**) in circumstances in which, as they were told from early directions hearings, their legal costs to trial were extremely likely to exceed any possible recovery. If the liquidators’ own time and costs were added to the legal costs then it must have been clear from the inception that this would eclipse any possible recovery. In some circumstances the public interest in recovery proceedings being brought by a liquidator might justify a risk being taken that legal costs might exceed recovery. But that public interest diminishes substantially where, as here, some of the liquidators’ claims are ambitious.

2 The liquidators claimed that FPJ Group was insolvent on 21 November 2013 so that $153,554 of payments after that date were unfair preferences under s 588FE of the *Corporations Act 2001* (Cth). However, on the face of things, the payments were part of a running account in a series of transactions. Unless this apparent fact could be met by the liquidators their claim was really one for $51,705.64. As might have been expected, their legal expenses alone were triple that amount.

3 From an early stage in the litigation, the liquidators also accepted that another part of their claim involved some ambitious submissions. This was the basis upon which they could deny a set-off in the amount of $43,738.86. Counsel for the liquidators accepted in an early directions hearing that the submission might require this Court to overturn, or depart from obiter dicta in a series of cases. As I explain later in these reasons, although the liquidators’ submissions did not refer to authority in any detail, the various submissions were inconsistent with two decisions of the Federal Court, four decisions of the New South Wales Supreme Court, and a decision of the New South Wales Court of Appeal. The leading commentator in the field of set-off, Dr Derham, has argued that many of these decisions are incorrect in various respects. But perhaps due to a view about the difficulties of making these submissions at first instance, counsel for the liquidators did not refer to any of Dr Derham’s arguments.

4 Despite the uncommercial nature of this litigation, the matter did not settle at mediation. The liquidators did considerable work on the case knowing that they would not be remunerated for that work unless they were successful.

5 In an attempt, no doubt, to reduce expense, one of the liquidators gave expert evidence in support of their case. His expert evidence aimed to show that FPJ Group was insolvent on 21 November 2013 and unable to pay its due debts on that date of $46,600. Unfortunately, due to the absence of evidence available to the liquidator concerning debtors and stock, the entirety of the liquidator’s expert evidence was based on a false assumption. The liquidator’s expert opinion on solvency was based upon whether there was ready cash available to cover the company’s commitments as they fell due for payment (ts 166). In *Rees v Bank of New South Wales* [1964] HCA 47; (1964) 111 CLR 210, 218, Barwick CJ said that solvency does *not* require “ready cash by him to cover his commitments as they fall for payment”. The liquidator had no records for stock and could not take any account of any stock on hand. The liquidator also was unaware of whether any related company might have lent money to FPJ Group on 21 November 2013. The liquidator had no record of the debts due to FPJ Group and so could not consider the value of any current debts owed to the company. Some current debts might have been demanded, especially if they were from related companies. They might have been able to be assigned to a financier immediately for value. They might have been released in exchange for a smaller payment. It cannot be assumed that the debts owed to FPJ Group on 21 November 2013 were small or even smaller than FPJ Group’s debts of $46,600 on that date. Indeed, at the time of winding up, the debts owed to FPJ Group were around $260,000 (ts 196).

6 Another obstacle to the liquidators’ case was that a payment will only be an unfair preference under s 588FA(1)(b) of the *Corporations Act* if there is a transaction which results “in the creditor receiving from the company, in respect of *an unsecured debt* that the company owes to the creditor, more than the creditor would receive from the company in respect of the debt if the transaction were set aside” (emphasis added). But the credit agreement between FPJ Group and CSR secured the debts.

7 One of the forms of security required by the credit agreement between FPJ Group and CSR was a retention of title clause over all the goods supplied until payment was received for them. Each payment of a debt to CSR had the effect of increasing the assets available to creditors by the same amount because the payment caused title to the goods to pass to FPJ Group. In *Airservices Australia v Ferrier* [1996] HCA 54; (1996) 185 CLR 483, 502, Dawson, Gaudron and McHugh JJ said that to “have the effect of giving the creditor a preference, priority or advantage over other creditors the payment must ultimately result in a decrease in the net value of the assets that are available to meet the competing demands of the other creditors”.

8 Despite the obvious difficulties for the liquidators’ case, and although the liquidators’ legal costs exceeded any possible recovery, counsel sensibly kept their costs to a minimum. Their submissions on the essential issues were very well presented and, properly, made with economy.

9 These reasons are divided by the issues as follows:

(1) The facts [12]-[51]

(2) The unfair preference provisions [52]-[56]

(3) The first issue: Was FPJ Group proved to be insolvent? [57]-[139]

(4) The second issue: Was FPJ Group’s debt secured? [140]-[180]

(5) The third issue: Did CSR receive more from FPJ Group than if the transaction were set aside? [181]-[188]

(6) The fourth issue: Did CSR act in good faith? [189]-[215]

(7) The fifth issue: Were the payments part of a running account? [216]-[225]

(8) The sixth issue: Does CSR have any set-off? [226]-[246]

10 The primary reasons why the liquidators’ application must be dismissed are in relation to the first and second issues. CSR’s defence on the fourth issue would not have succeeded. These matters were the focus of the trial (the second issue a little belatedly).

11 In the absence of submissions on important aspects of the third and sixth issues I do not express any final conclusions on these. It suffices to say that each of these issues also presented serious obstacles for the liquidators. Further, even if the liquidators had succeeded on all the other issues I have mentioned in this paragraph, they would have failed on the fifth issue and their claim would have been limited to an amount which would not have been more than $60,000 (excluding from the running account the debt for the final goods provided).

## Summary of the facts

### FPJ Group

12 FPJ Group started trading in late 2010. It had the trading name of Titan Building Supplies. FPJ Group’s business involved buying building supplies from suppliers and then selling them to builders.

13 FPJ Group was wound up in insolvency on 18 July 2014.

### The September 2010 Credit Agreement

14 On 26 September 2010, FPJ Group entered a credit agreement with CSR (**September 2010 Credit Agreement**). That credit agreement was comprised of a signed application for commercial credit and accompanying terms and a deed of guarantee and indemnity. The agreement included the following terms.

15 **Terms of credit**. The application provided that “You have received the terms of credit that were attached to this application. You agree to the terms of credit. You agree that you will pay by the last working day of the month after the month of invoice”.

16 The accompanying terms of credit provided that “You will settle your account at 30 days. We must receive your payment by the last working day of the month after the month of invoice. Any variation must be agreed in writing.”

17 **Retention of title**. The application also provided that “You agree that any goods you receive remain the property of CSR until CSR receives payment for them”. The application also provided that FPJ Group agreed to the terms of sale.

18 The accompanying terms of sale included the following clauses:

**3. We own the goods until they are paid for.** Goods supplied to you remain our property until we receive payment for all amounts you owe to us. If your account is in default we have the right to enter your premises (or the premises of any associated company or agent) to retake possession of the goods, without liability for trespass or damage. If you resell the goods, or if you sell products manufactured using the goods, then you must keep the proceeds of sale in a separate, identifiable account until we have been paid in full.

**4. Goods are at your risk** from the moment of delivery or collection. We are not liable for any claim or loss arising from the loading, transporting, or unloading of goods that you collected.

19 **Charge over land**. The terms of sale also provided that FPJ Group charged any real property in which it had an interest, as follows: “you now charge all real property in which you now or in the future have any title or interest with the payment of all money which shall be owing by you to us from time to time…”.

20 **Guarantee**. A guarantee was also provided as security for the debts incurred by FPJ Group. The guarantee was provided by Mr and Mrs Edwards.

### Payments to CSR by FPJ Group

21 Between January 2014 and June 2014, FPJ Group made a series of payments for building supplies. The effect of the retention of title clauses was that until those payments were made the title to the goods remained with CSR. A table of those payments is as follows:

|  |  |
| --- | --- |
| **The Alleged Preference Payments** | |
| **Date** | **Amount ($)** |
| 22/01/2014 | 5,770.01 |
| 29/01/2014 | 10,000.00 |
| 30/01/2014 | 3,000.00 |
| 30/01/2014 | 5,000.00 |
| 20/02/2014 | 5,085.32 |
| 20/02/2014 | 16,000.00 |
| 13/03/2014 | 6,555.44 |
| 18/03/2014 | 5,000.00 |
| 19/03/2014 | 7,000.00 |
| 21/03/2014 | 7,500.00 |
| 24/03/2014 | 7,500.00 |
| 14/04/2014 | 15,630.46 |
| 16/04/2014 | 5,000.00 |
| 24/04/2014 | 5,000.00 |
| 28/04/2014 | 5,000.00 |
| 29/04/2014 | 5,000.00 |
| 30/04/2014 | 14,000.00 |
| 7/05/2014 | 25,513.12 |
| **Total** | **153,554.35** |

22 At the commencement of the trial I raised with counsel a difficulty that appeared to arise in relation to the payments. There was no evidence, in any document or witness statement, that explained the goods to which each of these payments related. Nor was there any evidence of the contemporaneous documents which were exchanged at the time of the payments. During the trial, counsel for the parties very helpfully agreed that the following documents were representative of all of the transactions.

23 First, a purchase order was provided by FPJ Group to CSR. The purchase order from FPJ Group was on its own letterhead. In the purchase order, FPJ Group described the goods (including their product code) that FPJ Group required. FPJ Group also provided the number of units of those goods, and their price. A total price was provided in bold. At the foot of the purchase order, FPJ Group included the statement that “SUPPLY OF GOODS … IS DEEMED AS ACCEPTANCE OF THE PRICES ON THIS PURCHASE ORDER”.

24 Secondly, CSR would produce a picking slip and a delivery docket. The picking slip and delivery document described the goods that were delivered. There were spaces on those documents to be completed by FPJ Group upon delivery of the goods. Those spaces required signature of the person to which the goods were “picked by” and confirmation that the goods conformed to the description in the picking slip and delivery docket.

25 Thirdly, CSR would provide FPJ Group with an invoice and terms upon delivery of the goods. The first page of that invoice again repeated the description of the goods, their quantity, and the price. It provided for the total payable, including GST. The second page of the invoice provided for payment options and terms of sale.

26 The terms of sale included the following clauses in near identical terms to the September 2010 Credit Agreement:

**3. We own the goods until they are paid for.** Goods supplied to you remain our property until we receive payment for all amounts you owe to us. If your account is in default we have the right to enter your premises (or the premises of any associated company or agent) to retake possession of the goods, without liability for trespass or damage. If you resell the goods, or if you sell products manufactured using the goods, then you must keep the proceeds of sale in a separate, identifiable account until we have been paid in full.

**4. Goods are at your risk** from the moment of delivery or collection. We are not liable for any claim or loss arising from the loading, transporting, or unloading of goods that you have collected or following delivery.

27 There were no submissions made about which of these documents concluded the contract between the parties. It appears from the documents that the contract was concluded by delivery accompanied by acceptance of the terms contained in the picking slip, delivery docket, and terms of delivery. Even if the terms of delivery were subsequently provided they would have been incorporated into the contract by custom based on previous conduct of the parties. I therefore proceed on the same basis as the parties had assumed which is that each of the documents in the three steps described above was a contractual document.

### The evidence from the former manager of FPJ Group (Mr O’Toole)

28 The central witness called by the liquidators was Mr O’Toole. Mr O’Toole was an honest and wholly reliable witness.

29 Mr O’Toole was the manager of FPJ Group until around mid-2014. He has been involved in the building supplies business since 1994. In late 2010, Mr O’Toole asked an investor, Mr Edwards, to invest in a building supplies business. Mr Edwards invested $240,000 into the business and Mr O’Toole became responsible for all aspects of its day to day management. Mr Edwards made additional cash contributions to the business as sought by Mr O’Toole until the end of 2011.

30 Mr O’Toole described the manner in which FPJ Group operated. Most of its creditors required payment for goods within 30 days which followed the end of the month in which the goods were provided. Mr O’Toole said that FPJ Group would rarely operate within those terms. However, FPJ Group would almost always, or always, pay within 60 days after the end of the month (ts 86).

31 Mr O’Toole said that FPJ Group had an overdraft limit of $31,000 with its bank.

### The evidence from CSR’s Regional Credit Manager (Mr Sellick)

#### Mr Sellick’s role at CSR and his evidence generally

32 CSR’s central witness was Mr Sellick. He is CSR’s Regional Credit Manager for all of Queensland. Mr Sellick has worked in the credit control and risk management industry for the last 15 years. He has worked for CSR since December 2011.

33 CSR has between 500 and 1000 customer accounts in Queensland. Mr Sellick manages more than 100 of those accounts on a day to day basis (ts 95).

34 Mr Sellick said that he has direct contact with all those customers whose accounts are overdue. This can vary from 50 to 250 customers (ts 124). He contacted them when they were overdue within an allocated risk code. FPJ Group was a middle of the range customer but not a major customer.

35 Although I do not consider that Mr Sellick was dishonest, I have treated his evidence with serious caution. He was often evasive. He was extremely reluctant to say anything that he thought might damage his employer’s case. Even when confronted with blindingly obvious propositions which were against his employer’s interest he would either gloss his answers or take considerable time before expressing agreement to an undeniable proposition. Any matter which was in his employer’s interest was accepted with alacrity.

#### CSR’s credit processes

36 Mr Sellick explained that each month CSR sells up to $10 million of building products on credit to customers. The customers range from sole traders to large construction companies. Mr Sellick’s evidence was that credit management of those customers involves balancing the desires for (i) timely repayment, and (ii) maintaining good relationships with customers. His evidence about CSR’s credit processes was as follows.

37 CSR’s customers in the building industry often need additional time to pay beyond the usual 30 day terms offered by CSR. This is because customers are often waiting for payment themselves and their accounting cycle might not match that of CSR (for instance, where customers are not paid until the end of the month but CSR requires payment in the middle of the month). CSR has many customers who have periodic cash flow difficulties and Mr Sellick derives comfort in cases where the customer has a history of previous compliance with plans for payment and where there is regular friendly communication.

38 CSR also employed a long stop approach generally to risk management. That long stop was where a customer has not paid an account for more than 60 days. In that case a “stop” is put on the customer’s account. The customer cannot order any further goods until the debt is paid.

39 CSR uses a computer software package for credit management. That package permits CSR to allocate a risk code to customers. Mr Sellick’s evidence about the risk codes, particularly his oral evidence, was not entirely clear. There appears to be no rational sequence to the numbers in the risk codes. As best that they can be explained, the effect of the risk codes can be summarised as follows:

(1) risk code 13: the customer is given the usual 30 days from the end of the month plus three days’ grace;

(2) risk code 8: the customer is given the usual 30 days from the end of the month plus seven days’ grace;

(3) risk code 12: the customer is given the usual 30 days from the end of the month plus sixteen days’ grace; and

(4) risk code 17: matters concerning recovery from the customer are in the hands of solicitors.

#### Mr Sellick’s evidence about his extension of credit terms to FPJ Group

40 One of the most contentious aspects of Mr Sellick’s evidence was an oral agreement that he said that he reached with Mr O’Toole. Mr Sellick said that FPJ Group was initially required to comply with 30 day payment terms. This was a reference to the terms discussed above in the September 2010 Credit Agreement that CSR “must receive your payment by the last working day of the month after the month of invoice” and that “Any variation must be agreed in writing”. Mr Sellick said that in January or February 2013 he negotiated with Mr O’Toole by telephone a change to 45 day payment terms to assist the business. Mr Sellick said that there was a discussion about FPJ Group’s cash flow and about how Mr O’Toole was awaiting payment from his creditors. Mr O’Toole asked for additional time to repay. Mr Sellick said that he told Mr O’Toole that he would change the status of the account to allow 45 days of credit.

41 Mr Sellick had sworn three affidavits before he gave oral evidence. Mr Sellick conceded that none of them expressly mentioned the extension of credit terms to 45 days that Mr Sellick said had occurred in the telephone discussion. The extension of credit was not in writing as was required by the September 2010 Credit Agreement. He said that he never wrote the extension down. He said that he never told anyone in CSR about this. He kept a log of *some* of his telephone calls. He did not record the details of the discussion in this call in the log. And Mr O’Toole made no mention of the extension of terms to 45 days in his evidence. Mr O’Toole had said (at [21]) that he did not recall FPJ Group “having any agreement in place between it and any of its creditors that [FPJ Group] could pay those creditors otherwise than in accordance with the creditor’s stated trading terms”.

42 Despite my serious reservations about Mr Sellick as a witness, and despite the unsatisfactory nature of a number of aspects of his evidence, I accept Mr Sellick’s evidence on this point because it is supported by documentary evidence.

43 The documentary record which supports Mr Sellick’s evidence is CSR’s ledger which records the amount owing, payments, credit terms, and risk codes allocated to customers. In March 2012, CSR’s risk code for FPJ Group changed from risk code 8 to risk code 12, and the terms changed from 30 days from the end of the month for payment to 45 days from the end of the month. Risk code 8 was described in the records of CSR as “Normal (+7 days) Risk”. This meant that an “automatic hold” was put on the customer’s account after 7 days. CSR would not release goods to the customer. Risk code 12 was described in the records of CSR as “Normal (+16 days) Risk”. This involved an extended indulgence to 16 days beyond the period of 30 days from the end of the month.

44 In Mr Sellick’s affidavit evidence he said that he had changed FPJ Group’s risk code on 8 March 2012 to code 12 (an indulgence of 16 days) although in that affidavit he said that he could not recall the reason why he did this. Mr Sellick accepted, in response to a question in cross-examination, that there is no other reason why the risk code would have changed other than following his conversation with Mr O’Toole. I accept this evidence. Mr O’Toole rarely paid within the terms of 30 days after the end of the month, although he never (or almost never) exceeded 60 days from the end of the month. He regularly had conversations with Mr Sellick about payments by FPJ Group to CSR. Given the way in which Mr Sellick managed FPJ Group’s credit, it is inherently likely that he would have discussed the relevant payment by FPJ Group at around 45 days from the end of the month. It is unlikely that his decision to extend the credit of FPJ Group would have been made unilaterally and unlikely that it would not have been communicated to Mr O’Toole.

45 I note, in passing, that counsel for the liquidators did not submit that the requirement in the September 2010 Credit Agreement that any change in credit terms was required to be in writing could be varied (see, for instance, *Globe Motors, Inc v TRW Lucas Varity Electric Steering Ltd* [2016] EWCA Civ 396). Nor did counsel argue that the oral promise by Mr Sellick failed to vary the September 2010 Credit Agreement because it was unsupported by consideration (compare *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1989] EWCA Civ 5; [1990] 1 All ER 512). These matters can be put to one side because, on any view, the oral statement by Mr Sellick was a waiver of Mr O’Toole’s obligation to pay within the required period. That waiver was never revoked.

### The evidence from CSR’s accounts manager (Mr Mulholland)

46 Mr Mulholland is the accounts manager for CSR, based in Rockhampton. He has worked for CSR for 15 years. He was a very impressive witness. He was frank, forthright, and completely honest. I have no hesitation in accepting all of his evidence.

47 Mr Mulholland explained that in his role as account manager in Rockhampton he was responsible for some of CSR’s customers. In 2013 he managed 30 to 40 accounts in the region. One of those accounts was FPJ Group. Although credit issues were the concern of Mr Sellick, sales issues were the concern of Mr Mulholland.

48 Mr Mulholland’s dealings with FPJ Group were only ever with Mr O’Toole. He explained how Mr O’Toole placed orders with CSR’s Rockhampton store for fibre cement building materials. Mr Mulholland spoke with Mr O’Toole regularly, on average every fortnight. They discussed FPJ Group’s business and upcoming projects. Mr Mulholland also arranged for FPJ Group representatives to provide advice in relation to use of CSR’s products on building sites.

49 Mr Mulholland and Mr O’Toole would sometimes also discuss payment for goods. It was usually Mr O’Toole who raised this issue after Mr O’Toole had been telephoned or emailed by Mr Sellick. Mr O’Toole would usually explain that he was waiting on a payment from one or more of FPJ Group’s customers. Mr Mulholland did not consider these conversations to be unusual. Customers would sometimes contact him towards the end of the month and explain that they needed extra time for payment. He would refer them to Mr Sellick.

50 Mr Mulholland never had any concerns about FPJ Group’s solvency until 20 May 2014. On that date he became aware that FPJ Group was in financial distress. Mr O’Toole met with Mr Mulholland and told Mr Mulholland that staff at FPJ Group had been informed that it would be closing. Mr O’Toole told Mr Mulholland that this was due to the downturn in the market and the failure of financial backers to support the business. Mr Mulholland told Mr Sellick and Mr Sellick placed a manual stop on the account for FPJ Group (ts 151). For some reason, probably an administrative error, goods were nevertheless dispatched on 21 May 2014 (ts 210).

51 Although Mr Mulholland had no concerns about FPJ Group’s ability to pay its debts prior to 20 May 2014, he frankly acknowledged a number of matters. He accepted that from mid-2013 onwards there was a significant downturn in the market in Rockhampton. He also accepted that he did not have any other accounts who had failed to pay on time “to those numbers” (ts 212).

## The provisions concerning unfair preferences

52 Section 588FF of the *Corporations Act* provides as follows:

**Courts may make orders about voidable transactions**

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

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

…

(2) Nothing in subsection (1) limits the generality of anything else in it.

(3) An application under subsection (1) may only be made:

(a) during the period beginning on the relation-back day and ending:

(i) 3 years after the relation-back day; or

(ii) 12 months after the first appointment of a liquidator in relation to the winding up of the company;

whichever is the later; or

(b) within such longer period as the Court orders on an application under this paragraph made by the liquidator during the paragraph (a) period.

…

53 A “voidable transaction” is defined in s 588FE of the *Corporations Act* as follows:

**Voidable transactions**

(1) If a company is being wound up:

(a) a transaction of the company may be voidable because of any one or more of subsections (2) to (6) if the transaction was entered into on or after 23 June 1993; and

…

(2) The transaction is voidable if:

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

(b) it was entered into, or an act was done for the purpose of giving effect to it:

(i) during the 6 months ending on the relation-back day; or

(ii) after that day but on or before the day when the winding up began.

…

54 An “insolvent transaction” is defined in s 588FC of the *Corporations Act* as follows:

**Insolvent transactions**

A transaction of a company is an insolvent transaction of the company if, and only if, it is an unfair preference given by the company, or an uncommercial transaction of the company, and:

(a) any of the following happens at a time when the company is insolvent:

(i) the transaction is entered into; or

(ii) an act is done, or an omission is made, for the purpose of giving effect to the transaction; or

(b) the company becomes insolvent because of, or because of matters including:

(i) entering into the transaction; or

(ii) a person doing an act, or making an omission, for the purpose of giving effect to the transaction.

55 I deal with the meaning of insolvency below. The liquidators relied only upon the allegation that the payments were “insolvent transactions” because they were unfair preferences. The meaning of an “unfair preference” is contained in s 588FA of the *Corporations Act* as follows:

**Unfair preferences**

(1) A transaction is an unfair preference given by a company to a creditor of the company if, and only if:

(a) the company and the creditor are parties to the transaction (even if someone else is also a party); and

(b) the transaction results in the creditor receiving from the company, in respect of an unsecured debt that the company owes to the creditor, more than the creditor would receive from the company in respect of the debt if the transaction were set aside and the creditor were to prove for the debt in a winding up of the company;

even if the transaction is entered into, is given effect to, or is required to be given effect to, because of an order of an Australian court or a direction by an agency.

(2) For the purposes of subsection (1), a secured debt is taken to be unsecured to the extent of so much of it (if any) as is not reflected in the value of the security.

(3) Where:

(a) a transaction is, for commercial purposes, an integral part of a continuing business relationship (for example, a running account) between a company and a creditor of the company (including such a relationship to which other persons are parties); and

(b) in the course of the relationship, the level of the company's net indebtedness to the creditor is increased and reduced from time to time as the result of a series of transactions forming part of the relationship;

then:

(c) subsection (1) applies in relation to all the transactions forming part of the relationship as if they together constituted a single transaction; and

(d) the transaction referred to in paragraph (a) may only be taken to be an unfair preference given by the company to the creditor if, because of subsection (1) as applying because of paragraph (c) of this subsection, the single transaction referred to in the last-mentioned paragraph is taken to be such an unfair preference.

56 As I explain below, the parties focused their submissions on s 588FA(1) and, belatedly, s 588FA(2). Curiously, although the defendant relied upon a running account it did not expressly mention s 588FA(3) and did not consider the terms of s 588FA(3).

## Issue 1: Was FPJ Group insolvent on 21 November 2013 or subsequently?

57 The liquidators submitted that the FPJ Group was insolvent from 21 November 2013. Since the winding up began on 18 July 2014, the date of 21 November 2013 is within 12 months preceding that relation-back day (see s 9 of the *Corporations Act*). Hence, for the purposes of their application under s 588FF, if the liquidators can prove insolvency on 21 November 2013 then the liquidators have the benefit of the statutory presumption of insolvency in s 588E(3)(b) that “the company was insolvent throughout the period beginning at that time and ending on [18 July 2014]”.

### The test for insolvency

58 Section 9 of the *Corporations Act* provides that “insolvent” has the meaning given by s 95A(2). That subsection provides that a person who is not solvent is insolvent. The meaning of when a person is solvent is provided in s 95A(1) which is “if, and only if, the person is able to pay all the person’s debts, as and when they become due and payable”. This has been described as the “cash flow test” of insolvency. The test is *not* whether the alleged insolvent has an excess of assets over liabilities: *Bank of Australasia v Hall* [1907] HCA 78; (1907) 4 CLR 1514, 1528 (Griffith CJ). A “company may be at the same time insolvent and wealthy. It may have wealth locked up in investments not presently realisable”: *Re Tweed Garages Ltd* [1962] Ch 406, 410 (Plowman J). However, an examination of assets and liabilities may assist in answering the cash flow question because the cash flow position must be assessed by reference to the company’s financial position as a whole.

59 In *Rees v Bank of New South Wales* [1964] HCA 47; (1964) 111 CLR 210, 218 Barwick CJ said:

It is quite true that a trader, to remain solvent, does not need to have ready cash by him to cover his commitments as they fall due for payment, and that in determining whether he can pay his debts as they become due regard must be had to his realizable assets. The extent to which their existence will prevent a conclusion of insolvency will depend on a number of surrounding circumstances, one of which must be the nature of the assets and in the case of a trader, the nature of his business.

60 This passage has been quoted with approval on many occasions: *Davies v Chicago Boot Co Pty Ltd* [2011] SASC 27 [16] (Sulan J); *Lewis, in the matter of Damilock Pty Ltd (In Liquidation) ACN 008 083 985 v VI SA Australia Pty Ltd ACN 002 433 267* [2008] FCA 1801 [20] (Mansfield J); *Duncan v Commissioner of Taxation; in the matter of Trader Systems International Pty Ltd (in liq)* [2006] FCA 885 [36] (Young J); *Australian Securities & Investments Commission v Plymin* [2003] VSC 123; (2003) 175 FLR 124, 208 [373] (Mandie J); *Re Bird; Ex parte M & G Casabene & Sons* (1979) 39 FLR 281, 288 (Sweeney J); *Expo International Pty Ltd v Chant* [1979] 2 NSWLR 820, 838 (Needham J).

61 There is a difference between what is often described as “a temporary lack of liquidity” and insolvency. The colloquial reference to a lack of liquidity is often made to describe circumstances where a company cannot meet its debts from its most liquid assets (cash or cash equivalents) and does not wish to generate immediate liquidity by other means. For instance, a company with insufficient cash to repay its debts that are due on 1 January might have been able to obtain sufficient cash during December by selling longer term assets or by assigning debts that are due to it and are expected to be paid soon. A decision might be made not to sell assets or assign debts but instead to delay the repayment of the company debts. This does not mean that the company is insolvent. It could have paid its debts when they fell due but for trading reasons it chose not to do so.

62 The important point, therefore, is that insolvency is not limited to an assessment of a company’s cash or cash like assets. In *Sandell v Porter* [1966] HCA 28; (1966) 115 CLR 666, 670-671 Barwick CJ said:

Insolvency is expressed in s. 95 as an inability to pay debts as they fall due out of the debtor’s own money. But the debtor’s own moneys are not limited to his cash resources immediately available. They extend to moneys which he can procure by realization by sale or by mortgage or pledge of his assets within a relatively short time — relative to the nature and amount of the debts and to the circumstances, including the nature of the business, of the debtor. The conclusion of insolvency ought to be clear from a consideration of the debtor’s financial position in its entirety and generally speaking ought not to be drawn simply from evidence of a temporary lack of liquidity. It is the debtor’s inability, utilizing such cash resources as he has or can command through the use of his assets, to meet his debts as they fall due which indicates insolvency. Whether that state of his affairs has arrived is a question for the court and not one as to which expert evidence may be given in terms though no doubt experts may speak as to the likelihood of any of the debtor’s assets or capacities yielding ready cash in sufficient time to meet the debts as they fall due.

See also *Australian Securities & Investments Commission v Plymin* [2003] VSC 123; (2003) 175 FLR 124, 208-209 [373]-[374] (Mandie J).

63 There is considerable authority that supports the conclusion that an assessment of when debts are due and payable is based upon when those debts are *legally* due. In *Lee Kong v Pilkington (Australia) Ltd* (1997) 25 ACSR 103, 112, in the Full Court of the Supreme Court of Western Australia, Owen J said that whether or not a ‘debt’ is ‘due’ is to be determined with reference to the legally binding agreement between the parties and not with regard to any reluctance by creditors to enforce legal rights. In other words, it does not matter even if it is unlikely that a creditor will enforce its debt because the statutory test is whether the debt is due and payable. See also *Re Toowong Trading Pty Ltd (In Liq)* [1989] 1 Qd R 207, 211 (Ryan J); *Standard Chartered Bank of Australia Ltd v Antico (Nos 1 & 2)* (1995) 38 NSWLR 290, 331 (Hodgson J); *Southern Cross Interiors Pty Ltd (In Liq) v Deputy Commissioner of Taxation* (2001) 53 NSWLR 213, 224-225 [54] (Palmer J).

64 On the other hand, in *Manpac Industries Pty Ltd v Ceccattini* [2002] NSWSC 330; (2002) 20 ACLC 1,304, 1,310 [40]-[41] Young CJ in Equity repeated his earlier remarks in *Hamilton v BHP Steel (JLA) Ltd* (1995) 13 ACLC 1,548 as follows:

[40] … when one is applying the cash flow test, it is relevant to take into consideration the relationships between creditor and debtor, any agreement and the course of conduct. In *Hamilton* I indicated that that course of conduct may mean that despite what is written on the invoices etc as to time for payment, industry practice or dealings between the parties demonstrate that everyone accepts that debtors will often not pay creditors within normal trading terms. In business circumstances sometimes it is quite necessary in an industry which is experiencing recession because otherwise creditors may not be able to sell their product at all. Even though they would prefer people to stick to their 30-day terms it is better to have recalcitrant debtors than sell no product at all.

[41] What I said in *Hamilton* seems to have been developed into a much stronger statement by counsel in *Emwest Products Pty Ltd v Olifent* (1996) 14 ACLC 1,826, 1,832-1,833; (1996) 22 ACSR 202,209-210 and in *Southern Cross* at ACLC 1,520; ACSR 315.. However, if what is said in *Hamilton* is properly examined, it will be seen that the proposition expounded is not only quite in accordance with authority, but is also good commercial and legal commonsense.

65 I doubt whether Young CJ in Equity intended by these remarks to suggest that the test for insolvency permits debts to be disregarded if they are legally due for payment. Instead, the point that his Honour was making was that a course of conduct between the parties might reveal an implied waiver of the obligation to pay the debt when it falls due. That waiver can be revoked if it has not been relied upon but otherwise it operates as a doctrine “introduced by the law to prevent a man in certain circumstances from taking up two inconsistent positions ... It looks, however, chiefly to the conduct and position of the person who is said to have waived, in order to see whether he has ‘approbated’ so as to prevent him from ‘reprobating’”: *Expense Reduction Analysts Group Pty Ltd v Armstrong Strategic Management and Marketing Pty Limited* [2013] HCA 46; (2013) 250 CLR 303, 315-316 [31] (the Court) quoting *Craine v Colonial Mutual Fire Insurance Co Ltd* [1920] HCA 64; (1920) 28 CLR 305, 326 (the Court).

### FPJ Group’s failure to pay debts on time

#### FPJ Group’s failure to pay its tax debts

66 From the outset of its trading, FPJ Group did not always pay its debts when they fell due. On 11 June 2013, FPJ Group entered into an arrangement with the Australian Taxation Office for payment of an outstanding income tax liability. The required payments were $12,000 every month until 28 May 2014 with the last payment on that date being $2,038.75. When the outstanding tax was paid, it was paid from FPJ Group’s overdraft account.

67 Between early October 2013 and late November 2013, the manager of FPJ Group, Mr O’Toole, had conversations with the Australian Taxation Office in which he requested an extension of time to repay FPJ Group’s tax liability under the arrangement. On each occasion he explained that FPJ Group was struggling to meet the repayment arrangements. The payment which was due on 28 November 2013 was $12,000. This was in addition to a tax debt due on 21 November 2013 of $26,600.

#### The delayed payments of the alleged preferences in January 2014

68 As I have explained, FPJ Group consistently paid CSR’s debts later than they were due. Counsel for the liquidators relied particularly upon correspondence concerning late payments by FPJ Group in January 2014. These emails concerned the payment of the November 2013 invoice.

69 On 14 January 2014, Mr Sellick sent an email to FPJ Group requesting details of when the November 2013 invoice payment was going to be paid. At that time the payment was just about to fall due by reference to the 45 day period (Court Book 755).

Good Morning Paul,

With regards to the November account $23,770.01, can you advise payment details.

70 Mr O’Toole responded on the same day (Court Book 755):

Greg,

I have been back since Monday and I too am struggling to get money in. I will be hopeful to have fixed up by next Wednesday [sic]. I will keep you informed along the way.

71 On 22 January 2014, Mr Sellick sent another email enquiring about the November invoice which was then 8 days overdue following the 45 day period (Court Book 754):

Good Morning Paul,

Just touching base regards the November account payment, can you advise.

72 Three hours later, Mr O’Toole responded (Court Book 754):

Hi Greg,

I am still struggling to get money in. However I just put through $5770.01, leaving 18K left for November. Is that correct? I will keep getting it paid off as it comes in. Hopefully I will have better news by this Friday coming. You should get an email from the bank as payment confirmation of mentioned amount for today.

73 The payment of $5770.01 was the **first alleged preference payment**.

74 On 28 January 2014, Mr Sellick emailed again (Court Book 756). The payment was now almost 60 days after the invoice and nearly 15 days overdue from the 45 day terms:

Good Morning Paul,

Just touching base as orders are still being received, need to advise that the balance of the November account $18K needs to be paid by Friday 31.1.2014.

Otherwise, will be unable to supply further till the payment has been received - the debt will be 60dys + [sic].

75 Mr O’Toole responded (Court Book 759):

Greg,

I can guarantee it will be paid by this coming Friday. Hopefully after the conversation I just had with one of our outstanding customers, I can have it paid tomorrow.

76 Mr Sellick’s response was brief, “Cool. Thanks Paul” (Court Book 759).

77 On 29 January 2014, Mr O’Toole made a payment of $10,000. This was **the second alleged preference payment**. He wrote an email to Mr Sellick confirming that payment (Court Book 759):

Greg,

Another 10K paid this morning. I sent you an email from the bank, so you should receive it?

78 Two further payments were made by Mr O’Toole on 30 January 2014. These were the **third and fourth alleged preference payments**.

#### The delayed payments of the alleged preferences in February 2014

79 The communications in February 2014 concerned the December 2013 invoice from CSR.

80 On 10 February 2014, Mr Sellick emailed Mr O’Toole about that invoice. On 45 day terms the amount would not have yet fallen due. The email was as follows (Court Book 769):

Good Afternoon Paul,

Just chasing payment details for the December account $21,085.32, can you advise.

81 Shortly after, Mr O’Toole replied as follows (Court Book 768):

Greg,

I am again chasing money for this month. My hope is to have half of it paid by this Friday, than [sic] the balance as it comes in. I will keep in contact.

82 On 17 February 2014, the December account had fallen due by reference to the 45 day terms. Mr Sellick emailed Mr O’Toole to follow up on the outstanding December account (Court Book 768):

Good Morning Paul,

Can you update payment details for the December account, as still receiving orders.

Payment required by Friday 21.2.2014.

83 Later that day, Mr O’Toole replied as follows (Court Book 767):

Greg,

I will have this account paid in full by your below given due date. I would suggest the reason you are still seeing orders come through is because we have seen a large increase in orders to Titan. This is a good sign in my view. It means we will in turn be busier, meaning of course our orders with CSR will increase.

Your point is not lost on me re the account needing to be settled.

84 A few minutes later, Mr Sellick replied (Court Book 767):

Paul.

The only reason for my query is that, usually you pay half by the 15th & settle the balance before the end of mth [sic].

So with new orders received this morning & no payment, had to ask.

There are no issues about getting paid but, I need to know what is going on for when I am asked questions.

85 Mr O’Toole replied to this email as follows (Court Book 766):

Greg,

I know why you have asked. I also know you are only doing your job in that you will also have someone asking you. My frustration is not aimed at you. My frustration is aimed at the customers NOT paying us.

86 Mr Sellick’s reply was brief, “Paul, Mate as long as we are cool”, to which Mr O’Toole replied “Greg, No probs there. Trust me you are only picking up on my own frustrations with our own debtors list” (Court Book 765-766).

87 The next day, on 18 February 2014, Mr O’Toole emailed Mr Sellick saying (Court Book 765):

Greg,

Just letting you know I am on track to have this paid in full either on or before this Friday. I have had some good news come in from one of our customers, who owes a large amount. I will email through the EFT payment once paid.

88 Mr Sellick replied saying he appreciated the email. On 20 February 2014, Mr O’Toole confirmed with Mr Sellick that the account for December had been paid in full. This payment was done by two transfers which were the **fifth and sixth alleged preference payments**.

#### The delayed payments of the alleged preferences in March 2014

89 On 13 March 2014, Mr O’Toole emailed Mr Sellick in relation to the January 2014 invoices as follows (Court Book 779):

Greg,

$6555.44 just paid for Jan. Will have the balance completed of 27K by next Friday at the latest. My hope is to have it done by next Tuesday. I will keep in contact.

90 The payment of $6,555.44 was the **seventh alleged preference payment**.It was paid within the 45 day period for payment.

91 Mr Sellick replied saying that was fine (Court Book 779).

92 On 18 and 19 March 2014, Mr O’Toole made another two payments of $5,000 and $7,000 respectively. These were the **eighth and ninth alleged preference payments**.

93 On 21 March 2014, Mr O’Toole emailed Mr Sellick again (Court Book 770):

Greg,

Attached is another payment for $7500.00 bringing the Jan balance left owing at $7500.00. If I don’t have this fixed over the weekend it will be fixed by COB Monday 24th.

94 The payment of $7,500 was slightly late. It was, as Mr O’Toole promised, followed by another payment of $7,500 on 24 March 2014. They were the **tenth and eleventh alleged preference payments**.

#### The delayed payments of the alleged preferences in April 2014

95 On 7 April 2014, Mr O’Toole emailed Mr Sellick in relation to the February account saying (Court Book 778):

Greg,

I am hoping to have some of the account paid by this Friday coming and the balance paid before the end of the month. I know that is not ideal. I will keep you informed.

96 A payment by the end of the month would have been outside the 45 day credit period but within a 60 day period.

97 Mr Sellick replied (Court Book 777):

Morning Paul,

Should be ok.

Feb acct is $49,63.46 [sic], can I get half before easter & balance by the 30th, let me know.

98 Mr O’Toole replied saying he would work to meet that arrangement.

99 On 14 April 2014, Mr O’Toole made a payment of $15,630.46. This was the **twelfth alleged preference payment**.

100 On 16 April 2014, 24 April 2014, and 28 April 2014 Mr O’Toole made three payments of $5,000. These were the **thirteenth, fourteenth and fifteenth alleged preference payments**.

101 On 28 April 2014, Mr Sellick requested that Mr O’Toole confirm that the balance of the account ($24,000) would be paid by 30 April 2014 (Court Book 775). Mr Sellick had not included in his calculation the fifteenth alleged preference of $5,000.

102 On 29 April 2014 Mr O’Toole replied that another $5,000 had been paid that morning, and that Titan was on track to have the February account paid by the end of the month (Court Book 775). The payment on 29 April 2014 was the **sixteenth alleged preference payment**.

103 On 29 April 2014, Mr O’Toole confirmed with Mr Sellick that the balance of the February account would indeed be paid by the end of the month (Court Book 774). As Mr O’Toole promised, the remainder of the account was paid on 30 April 2014. This was the **seventeenth alleged preference payment**.

#### The delayed payments of the alleged preferences in May 2014

104 On 7 May 2014, Mr O’Toole made a payment of $25,513.12 in relation to the April invoices. This was the **eighteenth alleged preference payment**.

105 On 20 May 2014, Mr Sellick emailed Mr O’Toole to enquire about the remainder of the April and May accounts (affidavit of Mr Sellick p141):

Good Afternoon Paul,

Just got off the phone with Brad, who advised me that the owners are shutting the doors this month.

With regards to the account, April balance is $23,320.07 and May is $19,764.63, total payable $43,084.70. Do I speak with you regards payment for the account, can you advise.

106 Mr O’Toole replied as follows:

Hi Greg,

That is correct. The owners have given me a commitment and instructed me to pay all creditors within the current terms, and that is what I am going to do.

107 The liquidators do not assert that any payment made after 7 May 2014 was a preference.

### The expert evidence

#### The two expert witnesses (Mr Box and Mr Ross)

108 Two experts were called by the parties. Their oral evidence was given concurrently. Their written evidence was given as a joint report. The joint report summarised all of the other reports that the experts had provided and the parties agreed that it was expeditious for the written joint report to stand alone as the expert evidence.

109 CSR called Mr Box. He is a partner of the Forensic Consulting Division of Grant Thornton, chartered accountants. He has worked as an accountant for 24 years. He has been employed by Grant Thornton for 17 years in their Forensic Consulting Division. He gave evidence in a fair and balanced way. His ultimate conclusion, which I accept, was that it is not possible on the evidence before the Court (and the evidence provided to the experts) to determine whether FPJ Group was insolvent in November 2013.

110 The liquidators called Mr Ross. Mr Ross is one of the two plaintiff liquidators. He works in the insolvency division of Hall Chadwick. He has almost 20 years’ experience in financial reconstruction, recovery and management of distressed companies.

111 Although there was significant cross-examination about Mr Ross’ independence and impartiality, I am satisfied that he approached his evidence honestly. But Mr Ross was not independent. Nor was he impartial. He properly accepted that he was not merely a plaintiff in these proceedings, in his capacity as liquidator, but also that he had done considerable work which would not be remunerated if the liquidators were unsuccessful in the proceedings. Although Mr Ross was honest, and although he was aware of his obligations as an expert, the conflict which he faced as both expert and party was apparent at times in his evidence.

112 One example of Mr Ross’ conflict is that I asked him a series of questions about his investigations of Meldevaly Homes and Mr and Mrs Edwards, including whether they had funds to support FPJ Group (ts 63-64). After answering several times that they did not, Mr Ross eventually said that he had not specifically enquired about their access to funds around 21 November 2013. As I explain below, the bank statements for Meldevaly Homes show substantial funds moving in and out of its account around that date.

113 Another example is that Mr Ross had to be asked a number of times whether the knowledge of the debtors and inventory of a company is necessary to identify whether a company has adequate cash resources. The answer to this question in this case was obviously, “yes”. Inventory could be sold at short notice to realise cash. And debtors can be assigned for cash. But Mr Ross constantly avoided the question (ts 155-156). Eventually he answered that he disagreed that this was necessary because he said that his opinion was based on the cash flow test (ts 157). It was apparent that he understood the “cash flow test” that he applied to be a test of whether there was cash on hand to pay the company’s debts as and when they fell due.

#### Mr Ross applied the wrong test for insolvency

114 The fundamental reason why none of Mr Ross’ conclusions can be accepted is because he applied the wrong test for insolvency. The test that Mr Ross applied can be summarised in his statement that “I based my opinion on the cash flow test and the available resources, cash resources, to meet its debts as and when they fall due” (ts 157). Mr Ross accepted that he “applied a cash flow test … whether there was ready cash available to cover the company’s commitments as they fell due for payment” (ts 166).

115 As I have explained above, this is the wrong test for insolvency. A company is insolvent if it is unable to pay its debts as and when they become payable. The test is not whether a company is unable to pay its debts *by ready cash on hand* as and when they become payable.

#### Can an inference of insolvency be drawn?

116 Counsel for FPJ Group submitted (ts 4, 22 April 2016) that even if Mr Ross’ evidence were rejected, the court could reach a conclusion that FPJ Group was insolvent from 21 November 2013 by inference from the circumstances. Those circumstances include its late payments of its debts. Each of those late payments is considered below.

117 The primary reason why Mr Ross chose the date of 21 November 2013 as the date of insolvency was because this was the due date for PAYG for the month ending 31 October 2013. FPJ Group failed to pay its PAYG of $26,600 on 21 November 2013. Instead, on 26 November 2013, a payment arrangement was entered into with the Australian Taxation Office.

118 The arrangement reached with the Australian Taxation Office on 26 November 2013 does not preclude the PAYG debt being due, in full, on 21 November 2013. I reject Mr Box’s opinion to the contrary. The Australian Taxation Office Practice Statement Law Administration 2011/14 provides:

52 ... Some taxpayers may experience cash flow difficulties that will prevent them from paying their debt on time. In those instances the Commissioner will consider requests to accept payment of the debt by instalments over a period of time. Accepting payment by instalments provides the Commission with an alternative to more formal recovery procedures.

53 Section 255-15 of Schedule 1 to the [*Taxation Administration Act 1953* (Cth)] gives the Commissioner the power to permit taxpayers to pay an amount of tax-related liability by instalments under an arrangement whether or not the liability has already arisen.

54 An arrangement under section 255-15 of Schedule 1 to the [*Taxation Administration Act 1953* (Cth)]does not vary the time at which the amount is due and payable. Any GIC, if applicable, in respect of any unpaid amount of the tax-related liability, begins to accrue when the liability is due and payable under the relevant taxation law...

119 FPJ Group might have had a reasonable expectation that it could reach a payment arrangement with the Australian Taxation Office. This expectation might have been based on the Practice Statement, but was more likely to be based on the conversations that Mr O’Toole had with the tax office. But a reasonable expectation is not a waiver of the obligation to pay the tax debt. Prior to, and on, 21 November 2013, FPJ Group’s tax had been due and payable on 21 November 2013.

120 Counsel for the liquidators also pointed to the debt that FPJ Group owed to CSR on 21 November 2013. That was a debt for CSR’s October account, in the amount of $20,000.

121 The total debt that the liquidators allege that FPJ Group was unable to pay on 21 November 2013 was therefore $46,600 (ts 9, 26 April 2016). There are eight reasons why I am not satisfied that FPJ Group was unable to pay its debts of $46,600 on 21 November 2013.

122 **First**, there was no direct evidence about the bank account of FPJ Group on 21 November 2013. It was common ground that the bank account was in overdraft on 21 November 2013, and counsel for the liquidators asked Mr Box to assume that the account was in overdraft to the extent of $20,000 (ts 186-187). But FPJ Group had an overdraft of $31,000. So, on any view it had at least $11,000 of immediate cash with which to pay its debts of $46,600.

123 For reasons which are unclear, the liquidators chose to lead evidence only of FPJ Group’s bank account for the two months of December 2013 and January 2014 (until 5 February 2014). The opening balance in December 2013 was $42,560. The balance fluctuated widely in the two months from as high as $95,431 in credit on 6 January 2014 to a couple of occasions when the account was as low as $30,000 overdrawn.

124 **Secondly**, there was no evidence about FPJ Group’s relationship with its bankers nor any evidence of its bank account before 21 November 2013 or shortly after that date. Any inference about whether FPJ Group’s bank would have extended its overdraft briefly, or refused to extend its overdraft, would be pure speculation.

125 **Thirdly**, there was no evidence of what FPJ Group’s debtors were on 21 November 2013 or at any time close to then. Mr Ross gave evidence that he knew from FPJ Group’s records that at the date of winding up (18 July 2014) FPJ Group had $260,000 of debtors (ts 157). It is pure speculation to try to guess whether FPJ Group had debts of that size on 21 November 2013 but if it did then those debts would eclipse the $35,000 that FPJ Group would need (at most) to meet from non-cash realisable assets. Even on this speculation, it would be hard to imagine why some or all of those debts could not be called in to ensure payment of FPJ Group’s due debts.

126 Counsel for the liquidators pointed to Mr Ross’ evidence that at the date of winding up $185,000 of the $260,000 debt was due to FPJ Group from Meldavaly Homes, which is a related company to FPJ Group (ts 157). But even if it were possible to transplant the debt at the date of winding up to 21 November 2013 (which it is not), any sizeable sum owed by the related company, Meldavaly Homes, to FPJ Group might make any immediate call *more* likely rather than less likely. There was evidence that the bank account of Meldavaly Homes on 21 November 2013 commenced with $51,950.32. That is a sizeable sum from which any debts could be paid. Many debts were paid by Meldavaly Homes on that day. At the conclusion of the day it had $6,816.16. The next day it received deposits of $122,000.

127 **Fourthly**, Mr Ross gave evidence that in the period June/July 2014, the directors or their related entities withdrew approximately $170,000 from FPJ Group’s bank account (ts 157, 167). Mr O’Toole said that Mr Edwards had supported FPJ Group until 2012. As one of the directors who had later withdrawn large sums in June or July 2014, there may have been a prospect that Mr Edwards might have wanted to support the business if it were viable in November 2013. Again, the absence of any information about debts or inventory makes the assessment of the likelihood of that prospect impossible.

128 **Fifthly**, there is no evidence of the stock or inventory that FPJ Group held on 21 November 2013. If FPJ Group held a large amount of stock then it is possible that it might have been sold at short notice, at a discount if necessary, to pay the debts due. It is relevant that $20,000 of the debt related to stock over which CSR retained title, so it is possible that the stock being sold could include the very stock to which a large part of the debt related.

129 Counsel for the liquidators relied upon the decision of Barwick CJ in *Rees v Bank of New South Wales*. After the passage (at 218) quoted above, where Barwick CJ explained that insolvency is *not* a test of whether a trader has ready cash to cover commitments, the Chief Justice explained that the extent to which realisable assets such as stock will prevent a conclusion of insolvency will depend upon circumstances such as the nature of the assets and the nature of the business. In that case, the company sold food to retail outlets. As Barwick CJ concluded, the stock in trade was clearly not an asset which was available to be realised to meet current debts other than in the ordinary course of business.

130 **Sixthly**, even apart from the absence of evidence about inventory and debtors, the evidence about FPJ Group’s other assets and liabilities was confused in several important respects. For instance, Mr Ross said that at the time of the appointment of the liquidators there was a related party loan from Meldavaly Homes to FPJ Group of $800,000. But that loan was not recorded in the books of Meldavaly Homes (ts 164-165). A possible inference is that the liability did not exist in circumstances in which it was not recorded by the creditor.

131 **Seventhly**, although I accept that FPJ Group routinely paid its debts late, including entering into arrangements with the Australian Taxation Office in April 2013 and November 2013, it almost invariably met the payment arrangements that it made. It had also been trading profitably (and owing tax on profits for 2012 and 2013). It is also relevant that at 21 November 2013, Mr O’Toole did not approach Mr Edwards or any other person for funding for FPJ Group. Nor did Mr O’Toole seek to raise money to pay the company’s debts urgently.

132 As Mr Box explained, it is not uncommon for solvent companies to enter into payment arrangements with the Australian Taxation Office (ts 48-49). In this case, FPJ Group met its obligations under the payment arrangements. In relation to the November 2013 payment arrangement, the payments are set out below. The reference to “effective date” is the date on which a payment is received. The “process date” is the date that the Australian Taxation Office processed the payment:

|  |  |  |  |
| --- | --- | --- | --- |
| **Amount** | **Deadline** | **Process Date** | **Effective Date** |
| $6,000.00 | 20 December 2013 | 13 December 2013 | 12 December 2013 |
| $20,600.00 | 7 January 2014 | 7 January 2014 | 6 January 2014 |

133 Mr Ross said that although the payments were made on time, FPJ Group failed to meet other conditions of its payment plans because it failed to make all other tax lodgements and payments by their due dates. The payment arrangement contained the additional conditions that future lodgements must be made by the due dates, and all future payment obligations must be made by the due dates.

134 During the course of the payment arrangement, one further return was required to be submitted to by FPJ Group, being the November 2013 PAYG tax return. That was a payment of $5,848 which was due by 23 December 2013. It was paid on 12 December 2013. And future lodgements of tax returns occurred on time.

135 **Eighthly**, although FPJ Group often paid CSR outside the 45 day terms that had been agreed, the payments before and after 21 November 2013 were almost always made as Mr O’Toole promised. Although FPJ Group routinely paid its accounts after the 45 day credit terms, and very often after the 30 day written terms, this was common in the building industry and it is not a strong indicator of insolvency in that industry. In the months between December 2013 and April 2014, there were between 65% and 72% of customers who paid between 30 and 60 days. On average, CSR’s credit customers paid their invoices between 50 and 53 days. The timing of payments that CSR customers made are set out in the table below:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Month of CSR invoices** | **Amount of credit sales** | **Paid within 30 days** | **Paid 31 days to 60 days** | **Paid 61 days+ or unpaid** |
| December 2013 | $4,742,882 | $1,204,092  (25.38%) | $3,369,266  (71.04%) | $169,524  (3.58%) |
| January 2014 | $6,261,936 | $1,441,647  (23.02%) | $4,496,344  (71.80%) | $323,945  (5.17%) |
| February 2014 | $7,387,555 | $1,964,620  (26.59%) | $4,983,759  (67.46%) | $439,176  (5.94%) |
| March 2014 | $7,243,855 | $1,801,963  (24.88%) | $4,707,089  (64.98%) | $734,803  (10.14%) |
| April 2014 | $6,132,924 | $1,412,259  (23.03%) | $4,515,020  (73.62%) | $205,645  (3.35%) |
| May 2014 | $7,761,095 | $2,122,505  (27.34%) | $5,147,493  (66.32%) | $491,097  (6.33%) |
| June 2014 | $7,335,378 | $1,778,841  (24.25%) | $5,346,452  (72.89%) | $210,085  (2.87%) |
| July 2014 | $8,757,357 | $1,907,777  (21.78%) | $6,365,756  (72.69%) | $483,824  (5.52%) |

### Conclusions on insolvency

136 All of these eight matters make an inference of insolvency extremely difficult, if not impossible, to draw. This is so even in light of matters which illustrate the very difficult nature of the business for FPJ Group. The economic conditions in Rockhampton where FPJ Group traded were difficult in 2013. I have also taken into account that Meldavaly Homes was one of FPJ Group’s largest customers and it conducted business in Emerald where business was even more difficult than Rockhampton due to a mining downturn and the lack of purchases of residential property.

137 I also take into account the disorganised nature of FPJ Group’s accountancy practices. Apart from its late payment of debts to CSR, and its late payment of the Australian Taxation Office debts that I have described, it failed to lodge and maintain its superannuation statutory obligations on a number of occasions. One of those was a Superannuation Guarantee Charge for the period ended March 2013 referred to by Mr Ross, although that was for only $23.42.

138 Ultimately, I consider that although there is a possibility that FPJ Group might have been insolvent in November 2013, and although FPJ Group clearly was not in a strong financial position in November 2013, there is insufficient evidence before me from which I can draw an inference of insolvency at any time prior to late May 2014.

139 In reaching this conclusion I also emphasise that the liquidators’ case focused almost exclusively on the position at 21 November 2013. The liquidators did not refer to any other date, including during the period of the alleged preference payments, when FPJ Group was said to be insolvent.

## Issue 2: Were FPJ Group’s debts to CSR unsecured?

### The issue

140 As I have explained in the section of these reasons dealing with the unfair preference provisions, s 588FA(1)(b) requires that an unfair preference be a transaction that “results in the creditor receiving from the company, *in respect of an unsecured debt* that the company owes to the creditor, more than the creditor would receive from the company in respect of the debt if the transaction were set aside and the creditor were to prove for the debt in a winding up of the company” (emphasis added).

141 CSR pleaded two matters in [11] of its amended defence in response to the liquidator’s allegation that CSR’s payments were in relation to an unsecured debt by FPJ Group. The first was that FPJ Group had granted a security to CSR pursuant to the September 2010 Credit Agreement. The second was that CSR had retained title to the goods that it supplied to FPJ Group under the September 2010 Credit Agreement.

142 The first pleading in defence can be dealt with briefly. As the liquidators anticipated in submissions, there are only two possible arguments that the debt was secured, apart from the retention of title clauses. One is that the debt was secured by a charge that CSR had over any real property held by FPJ Group. The liquidator submitted that FPJ Group owned no real property. CSR did not dispute this in its pleading or in oral submissions. The second argument is that the guarantee that was given by Mr Edwards was a security. This point was not pressed by CSR (ts 44, 22 April 2016).

143 The issue became a question of whether a retention of title clause had the effect that the debt owed by FPJ Group was not “unsecured”.

### The retention of title clause means that the debt is secured

#### (1) An “unsecured debt” is not defined in s 588FA(1)(b) and could encompass retention of title

144 The *Corporations Act* does not define the term “unsecured debt” which is used in s 588FA(1)(b). For the following reasons, there is no difficulty in the undefined term including a retention of title clause.

145 The concept of a “secured debt” can have different meanings in different contexts. In *General Motors Acceptance Corp Australia v Southbank Traders Pty Ltd* [2007] HCA 19; (2007) 227 CLR 305, 312 [20], the High Court of Australia in a joint judgment explained that the word “secures” can be used in a broad or a narrow sense. In a broad sense it could include a guarantee from a third party (citing *Singer v Williams* [1921] 1 AC 41, 49 (Viscount Cave). The Court continued (312-313 [20]-[21], footnotes omitted):

20 … In the same case, Lord Shaw of Dunfermline said:

“The word ‘securities’ has no legal signification which necessarily attaches to it on all occasions ... and it is to be interpreted without the embarrassment of a legal definition and simply according to the best conclusion one can make as to the real meanings of the term as it is employed in, say, a testament, an agreement, or a taxing or other statute as the case may be.”

21 The potential width of the term “security” is reflected in the meaning given in *Stroud’s* *Judicial Dictionary* as “anything that makes the money more assured in its payment or more readily recoverable.” In *Butterwo**rths Australian Legal Dictionary*, with reference to *Batchelor & Co Pty Ltd v Websdale*, the word “security” is primarily defined as “something that secures or makes safe.”

146 In *General Motors Acceptance Corp Australia,* the High Court held that the reference in s 3(1) of the *Chattel Securities Act 1987* (Vic) to an interest which “secured the payment of a debt” was broad enough to include a conditional sale where title to the property did not pass to the purchaser.

147 This conclusion that a retention of title clause can be described as a “security” is long established. In the leading case from which retention of title clauses got the name “Romalpa clauses”, *Aluminium Industrie Vaassen BV v Rompala Aluminium Ltd* [1976] 2 All ER 552, Roskill LJ explained at 562:

It is obvious, to my mind, that the business purpose of the whole of this [retention of title] clause… was to secure the plaintiffs, so far as possible, against the risks of non-payment… The plaintiffs were to be given the ownership of these mixed or manufactured goods as ‘surety’ for ‘full payment’. ‘Surety’ I think in this context must mean, as counsel for the plaintiffs contended, ‘security’.

148 In *Associated Alloys Pty Ltd v Metropolitan Engineering & Fabrication Pty Ltd (Voluntary Administrators Appointed) (Receivers and Managers Appointed)* (1998) 16 ACLC 1633, 1637, in a passage not discussed on appeal to the High Court (see *Associated Alloys v ACN 001 452 106 Pty Ltd (in liq)* [2000] HCA 25; (2000) 202 CLR 588) Sheller JA (Beazley and Stein JJA agreeing) said:

The Romalpa clause was developed to protect the unpaid seller of goods from the consequences of the buyer’s insolvency by the simple expedient of providing that the seller would retain title in the goods until they were paid for; *Armour v Thyssen Edelstahlwerke AG* [1991] 2 AC 339 at 352-3.

#### (2) Treating retention of title as securing a debt is consistent with the 2010 amendments

149 Although the *Corporations Act* does not contain any definition of “unsecured debt”, in 2010 a definition of “security interest” was introduced. That definition was introduced into s 51 of the *Corporations Act* to give effect to the *Personal Property Securities Act 2009* (Cth). The definition of “security interest” is not a definition of “unsecured debt” but it provides context for the construction of the meaning of “unsecured debt”.

150 Section 51 was introduced into the *Corporations Act* by the *Personal Property Securities (Corporations And Other Amendments) Bill 2010* (Cth). In his second reading speech, Dr Emerson said:

Second, the amendments will amend the terminology of the Corporations Act to make it consistent with the PPS [*Personal Property Securities*] Act. This will include removing the distinction between different forms of security interest, so as to treat transactions that secure payment or performance of an obligation as security interests, regardless of their legal form.

The third objective is to ensure the Corporations Act treats property provided by a supplier on a ‘retention of title’ basis as secured property. Many businesses supply goods on this basis, retaining title to the goods until the purchase price is paid. Treating such supplies as secured property is consistent with the PPS scheme’s approach of treating transactions that in substance secure payment or performance of an obligation the same way, regardless of the form of the transaction.

See Commonwealth, *Parliamentary Debates*, House of Representatives, 10 March 2010, 2009 (Dr Craig Emerson).

151 Although the retention of title clause in the September 2010 Credit Agreement between CSR and FPJ Group does not fall within the definition of a “security interest” in s 51 of the *Corporations Act,* this is only because of the timing of that agreement (as a “transitional security interest”). The timing does not prevent the retention of title clause in that agreement from negating the “unsecured” nature of FPJ Group’s debts. If it did so then it would be inconsistent with the emphasis upon substance over form that was promoted by the 2010 amendments. In order to explain this point, it is necessary to explain why the retention of title clause in the September 2010 Credit Agreement is not a “security interest” as defined.

152 Section 51E of the *Corporations Act* provides that a “secured creditor” of a corporation means a “creditor of the corporation, if the debt owing to the creditor is secured by a security interest”. Section 51A provides that a security interest means a “(a) a PPSA security interest” or “(b) a charge, lien or pledge”. A “PPSA security interest” is defined in s 9 as having the meaning given to it in s 51.

153 Section 51 defines a “PPSA security interest” as follows:

(short for Personal Property Securities Act security interest) means a security interest within the meaning of the *Personal Property Securities Act 2009* and to which that Act applies, other than a transitional security interest within the meaning of that Act.

154 Section 12(1) and 12(2)(d) of the *Personal Property Securities Act 2009* (Cth) provide that a “security interest” under that Act means “an interest in personal property provided for by a transaction that, in substance, secures payment or performance of an obligation” and includes “an agreement to sell subject to retention of title”. The retention of title clauses in the September 2010 Credit Agreement are therefore a “security interest” within the *Personal Property Securities Act.*

155 Section 308(a) of the *Personal Property Securities Act* provides that a “transitional security interest” arising before the registration commencement time means a security interest provided for by a transitional security agreement, if the *Personal Property Securities Act* would have applied in relation to it but for s 310. This introduces two concepts for a “transitional security interest”:

(1) a “transitional security agreement”; and

(2) the registration commencement time.

156 The September 2010 Credit Agreement is a transitional security agreement which gives rise to a transitional security interest before the registration time for the following reasons.

157 Section 307 of the *Personal Property Securities Act* defines a “transitional security agreement” as a “security agreement that is in force immediately before the registration commencement time, and that continues in force at and after that time”. The *Personal Property Securities Act* was assented to on 14 December 2009. By s 306(2)(b), the registration commencement time was 30 January 2012. The September 2010 Credit Agreement between CSR Building Products and FPJ Group commenced on 26 September 2010.

158 Section 310(d) then has the effect that the *Personal Property Securities Act* applies at the commencement date for a “transitional security interest” that arises before the registration commencement time. Section 322(1) then provides:

A transitional security interest in collateral is perfected from immediately before the registration commencement time, whether the security interest arises before, at or after the registration commencement time ...

159 Since the retention of title clause in the September 2010 Credit Agreement is a “transitional security interest”, it is excluded from being a “security interest” under s 51A of the *Corporations Act*.

#### (3) Other provisions of the Corporations Act which treat retention of title as securing a debt

160 The *Corporations Act* contemplates that debts might be subject to retention of title clauses. Section 9 of the *Corporations Act* defines a “retention of title clause” as follows:

property is subject to a ***retention of title clause*** under a contract for the sale of property:

(a) if the contract contains a provision the effect of which is that the seller retains title in the property until the purchase price, or another amount, has been paid in full; and

(b) if the purchase price, or the other amount, as the case may be, has not been paid in full; and

(c) to the extent that the contract does not give rise to a PPSA security interest in the property.

161 In some provisions of the *Corporations Act,* a retention of title clause is treated in the same way as a “security interest” (as defined) even where the retention of title clause does not fall within the definition of “security interest”. For instance, s 442CB has the effect that an administrator must act reasonably in disposing of property for sale if the property is subject to a security interest *or* if it is subject to a retention of title clause. Section 442CC also treats in similar respects a possessory security interest with a retention of title clause for the purposes of determining the distribution of proceeds from the sale of property by an administrator.

162 Another statutory indication that a retention of title secures a debt to which it relates within s 588FA is the operation of s 442CC of the *Corporations Act*. That section is concerned with proceeds from the sale by an administrator of property which is the subject of a “possessory security interest”, “PPSA retention of title property”, and “Property subject to a retention of title clause”.

163 Section 442CC(2) provides (emphasis added):

…

Property subject to a retention of title clause

(2) If:

(a) a company is under administration; and

(b) property is used or occupied by, or is in the possession of, the company; and

(c) another person is the owner of the property; and

(d) the property is subject to a retention of title clause under a contract (the ***original contract***); and

(e) the administrator disposes of the property by way of sale;

then:

(f) if the net proceeds of sale equals or exceeds the total of:

(i) so much of the purchase price, or other amount, under the original contract as remains unpaid; and

(ii) if there are one or more securities over the property--the debts secured by the securities;

the administrator must:

(iii) set aside so much of the net proceeds as equals that total; and

(iv) apply the amount so set aside in paying that total; or

(g) if the net proceeds of sale fall short of the total of:

(i) so much of the purchase price, or other amount, under the original contract as remains unpaid; and

(ii) if there are one or more securities over the property-the debts secured by the securities;

then:

(iii) the administrator must set aside the net proceeds; and

(iv) the administrator must apply the amount so set aside in paying those debts in order of priority, on the basis that if the amount is insufficient to fully pay debts of the same priority, they must be paid proportionately; and

(v) if any of those debts is not fully paid-so much of the debt as remains unpaid may be recovered from the company as an unsecured debt.

164 The effect of s 442CC is to confirm that, in relation to an administrator, a retention of title clause has the effect that the debt is *not* an unsecured debt. This is because the proceeds of sale of property subject to a retention of title clause are to be paid to satisfy the unpaid debt before secured creditors and before any “unsecured debt”.

#### Conclusion on the retention of title clause as security

165 The three matters above all point to retention of title clauses being a security for the purposes of s 588FA(1)(b). It was not pleaded, nor submitted by counsel for the liquidators, that the retention of title clause in the September 2010 Credit Agreement (as a “transitional security”), or as the terms of any of the particular purchases of goods, were unenforceable because they were not registered under the *Personal Property Securities Act.* Counsel for the liquidators specifically abandoned any reliance upon s 267A of the *Personal Property Securities Act* (ts 21, 22 April 2016); see also *Central Cleaning Supplies (Australia) Pty Ltd v Elkerton* *(in his capacity as joint and several liquidator of Swan Services Pty Ltd (in liq))* [2015] VSCA 92; (2015) 321 ALR 181.

166 As a matter of purposive operation of s 588FA(1)(b), the contrary conclusion would also lead to very surprising results. If a retention of title clause were enforceable, but not a security within s 588FA(1)(b), then the creditor could potentially recover the goods but remain an unsecured creditor for the purposes of proving in the insolvency. As Bathurst CJ (Beazley JA and Tobias AJA agreeing) said in *Roberts v Investwell Pty Ltd (in liq)* [2012] NSWCA 134; (2012) 88 ACSR 689, 698 [31]:

the question depends, in my view, on the construction of the clause in question. If the provision on its true construction confers an immediate equitable interest in particular property, or grants an immediate right of recourse to present or future property, then the grantee will be secured to the extent of his or her interest in, or right to, the property. If it does not, the creditor will be unsecured.

167 Once the liquidators had conceded that a retention of title clause is a security within s 588FA(1)(b), counsel for the liquidators shifted course in closing submissions. He submitted that the payments could only be preferences to the extent that the payments exceed the value of the supplied asset retained by FPJ Group at the date of winding up (ts 15-16, 22 April 2016). I turn now to that submission.

### The value of the security under s 588FA(2)

168 Counsel for the liquidators submitted in closing that the debt owed to CSR was unsecured because of the operation of s 588FA(2) which provides that “for the purposes of subsection (1), a secured debt is taken to be unsecured to the extent of so much of it (if any) as is not reflected in the value of the security”. Counsel submitted that the “value of the security” was a matter to be determined at the date of winding up (ts 13-15, 22 April 2016). He submitted that at the date of winding up FPJ Group had sold all of the assets subject to the security so that the value of the security was zero.

169 There are five reasons why this submission must be rejected. There may be a sixth, which I consider below but do not decide.

170 **First**, this issue was not pleaded in reply by the liquidators. CSR had not admitted that the preference payments were in relation to an “unsecured debt”, and it had specifically pleaded in defence to this that it “retained title to items supplied to FPJ Group until they were paid for by FPJ Group” ([11(b)]). At no stage prior to oral closing submissions did the liquidators assert that the retention of title was a security of no value because the goods had all been sold.

171 **Secondly**, and consequent upon the first point, there was no evidence led about whether or not any or all of the goods had been sold. All that counsel for the liquidators could say in closing submissions was that it was “highly unlikely that any of the original supplies remained” (ts 20, 22 April 2016). This might be true in relation to some of the early supplies. But it is hard to see how any inference could be drawn in relation to, for example, the goods which were the subject of the $25,513.12 payment on 7 May 2014, when the company ceased to trade later that month.

172 **Thirdly**, even if an inference could be drawn that all of the goods had been sold by FPJ Group, the failure of the liquidators to plead this matter or to raise it earlier has had the effect of precluding CSR from exploring other issues. For instance, issues might have arisen concerning whether CSR retained title to any goods sold where only part of the payment had been made for those goods. Would a claim by CSR to title over goods held by a third party amount to security in those circumstances? The failure of the liquidators to allocate payments to goods that were supplied also precluded an examination of this issue.

173 **Fourthly**, and further to the third point, if this point had been pleaded in reply by the liquidators or had been raised at any point prior to oral closing addresses then it might have been met with a response that the full terms of the retention of title clause provide that “[i]f you resell the goods, or if you sell products manufactured using the goods, then you must keep the proceeds of sale in a separate, identifiable account until we have been paid in full”. In *Associated Alloys v ACN 001 452 106 Pty Ltd* [2000] HCA 25; (2000) 202 CLR 588 the High Court held that a clause of a security, which included the subclause below (at 597 [9]), created a trust of the proceeds:

The [Buyer] will receive all proceeds whether tangible or intangible, direct or indirect of any dealing with such goods/product in trust for the [Seller] and will keep such proceeds in a separate account until the liability to the [Seller] shall have been discharged.

174 In this case, no submissions were made about whether the retention of title clause created a trust but it is, at least, arguable that on its proper construction the meaning of the requirement for a separate account was to create a trust of those proceeds for CSR which is defeasible only upon payment for the goods.

175 **Fifthly**, assuming that the liquidators are correct in their assumption that the value of the security is to be determined at the date of winding up, that exercise of calculating value would need to focus on the value of a *notional* security at the date of winding up. Any alleged preference payment that was secured would discharge the security at the date of the alleged preference payment. For instance, suppose a debt were secured by a charge over freehold title to land that has the same value as the debt. The repayment of the debt would discharge the charge. At the date of winding up, the charge no longer exists. The “value of the security” at the date of winding up could only be the value of a notional security that would have existed at the date of winding up in the same terms as the charge which has been discharged. This exercise in determining the notional value of the security should not be affected by whether the freehold title, after release from the charge, had been sold by the company especially if the sale would not have been possible without the payment of the debt and discharge of the charge. The same must be true of a retention of title security.

176 **Sixthly**, it is arguable that the liquidators are incorrect in their assumption that the value of the security is a matter to be determined at the date of winding up. Since this issue was only raised in closing submissions, counsel were only able to make brief submissions about whether the “value of the security” is a matter to be determined at the date of winding up or at the date of the transaction. Counsel for CSR submitted that it should be determined at the date of the transaction.

177 Curiously, there appears to be very little authority on this proposition. Counsel for the liquidators said that the only authority which had decided this point (and held that the time to assess the value of the security is the date of winding up of the company) was a decision of the South Australian District Court in *Matthews v The Tap Inn* [2015] SADC 108. Unfortunately, counsel for the liquidators did not appear to be aware that the decision was set aside by the Full Court because it had been decided on a hypothetical basis: *The Tap Inn Pty Ltd v Matthews* [2015] SASCFC 188. Nevertheless, it is noteworthy that in that case the primary judge said that the question had not been considered before (see [13]).

178 There are reasons to favour the submission of the liquidators on this issue. One reason is that their submission is supported by the rationale of the preference provisions in s 588FA. In *BP Australia Ltd v Brown* [2003] NSWCA 216; (2003) 58 NSWLR 322, 342 [92]-[93], Spigelman CJ said that the focus of the provisions concerning preferences is “upon the interrelationship of creditors inter se” and that “the longstanding principle of equality between creditors applies”. That principle of equality applies at the date of winding up, not at an earlier date by which a “notional winding up” would be assessed for the purposes of calculating the value of the security: see also *Walsh v Natra Pty Ltd* [2000] VSCA 60; *Williams (as liquidator of Scholz Motor Group P/L (in liq)) v Peters* [2009] QCA 180; (2009) 232 FLR 98.

179 But there are also arguments to the contrary. One contrary argument is the effect of a finding that an unfair preference under s 588FA is a voidable transaction if it falls within s 588FE. A court may make an order in relation to a voidable transaction under s 588FF(1)(c) that requires a person to pay to the company “an amount that, in the court’s opinion, fairly represents some or all of the benefits that the person *has received* because of the transaction” (emphasis added). If the orders to unwind a voidable transaction on this ground were read literally to focus on the benefits that the person *has received* (rather than “has received and retains”), then symmetry should require that the security that the person held should also be assessed at the time of the transaction. However, it may be that this argument would be affected by the third issue discussed below.

180 In the absence of any submissions on these issues, I do not decide this point. It suffices to say that I reject the liquidators’ submission for the previous five reasons.

## Issue 3: Did CSR receive more from FPJ Group than if the transaction were set aside?

181 Even if much of the value of the security of the retention of title clause were deemed to be “unsecured” by s 588FA(2), there is another strong argument which might have been made for why the liquidators’ claims must fail. This argument is that the liquidators did not prove that CSR would receive more from FPJ Group by the preference payments than if the transaction were set aside and CSR were to prove for the debt in a winding up. Since this point was not pleaded and was only dealt with peripherally in submissions it suffices to explain it briefly.

182 To reiterate, s 588FA(1)(b) of the *Corporations Act* provides that a transaction is an unfair preference only if various requirements are met, including that “the transaction results in the creditor receiving from the company, in respect of an unsecured debt that the company owes to the creditor, more than the creditor would receive from the company in respect of the debt if the transaction were set aside and the creditor were to prove for the debt in a winding up of the company”.

183 The term “transaction” is defined in s 9 of the *Corporations Act* for the purposes of the provisions in Part 5.7B (which includes the voidable transaction provisions) as follows:

***“transaction”***, in Part 5.7B, in relation to a body corporate or Part 5.7 body, means a transaction to which the body is a party, for example (but without limitation):

(a) a conveyance, transfer or other disposition by the body of property of the body; and

(b) a security interest granted by the body in its property (including a security interest in the body’s PPSA retention of title property); and

(c) a guarantee given by the body; and

(d) a payment made by the body; and

(e) an obligation incurred by the body; and

(f) a release or waiver by the body; and

(g) a loan to the body;

and includes such a transaction that has been completed or given effect to, or that has terminated.

184 This definition of transaction, as a “transaction to which the body is a party” is circular. Section 9 provides examples of a transaction rather than defining it. As the Full Court said in *Re Emanuel (No 14) Pty Ltd (in liq); Macks v Blacklaw & Shadforth Pty Ltd* (1997) 147 ALR 281, 288, the examples have a common characteristic “that the conduct or dealing engaged in by the debtor company has the consequence of effecting a change in the rights, liabilities or property of the company itself”. The Court continued, explaining that the transaction is “the totality of the dealings initiated by the debtor so as to achieve the intended purpose of extinguishing the debt”.

185 The relevant “transactions” upon which the liquidators relied were the 18 alleged preference payments. Those transactions resulted in FPJ Group making the various payments. But the totality of the dealing also *resulted* in CSR *losing* title to the goods to which the payments related. There was no suggestion that the title to the goods was worth less than the amount that FPJ Group paid. The *net* receipt to CSR from the transaction was nothing.

186 There may have been two ways in which this argument could have been met by the liquidators. The first is by a submission that s 588FA is concerned only with the benefit that the creditor immediately receives from the transaction so that any loss to the creditor is ignored. This submission was not made. It would be a difficult argument. It would be inconsistent with the approach to “transaction” taken in *Re Emanuel.* It would require a narrow construction of the word “results”. And it is hard to see how a payment which results in no net benefit to a creditor could be a preference. The same principle might be said to underlie the requirement in s 588FG(1)(a) that a court is not to make an order under s 588FF “materially prejudicing a right or interest of a person other than a party to the transaction if it is proved that the person received no benefit because of the transaction”.

187 The second argument that the liquidators might have made is that *some* of the payments did not discharge the whole of the debt for a particular item of property. Hence, if each payment could be considered in isolation *and* if CSR did not lose title in relation to some of the goods because the individual payment did not discharge the debt in relation to the goods that were held, then that payments could be a preference. Such a submission would be dependent upon the form of the transaction so that a series of payments of the same invoice are seen as a series of transactions rather than one transaction. This may be inconsistent with the conclusion in *Re Emanuel* (287-289) that a composite of dealings can be a transaction. More significantly, it would require the payments to be matched to the invoices so that the liquidators could identify which payment resulted in no net benefit to CSR and which resulted in a new benefit to CSR. Although I urged the liquidators at the start of trial to perform this exercise they chose not to do so.

188 It is not necessary to reach any conclusion on this matter and, in the absence of full submissions on the point, I do not reach any final conclusion. It suffices to say that if I had reached the conclusion that the debt was unsecured I would have sought further submissions from the parties on this legal issue. There is a real likelihood that the liquidators would also have failed to prove this aspect of their claim.

## Issue 4: Does CSR have a “good faith” defence?

189 The first defence relied upon by CSR is the defence contained in s 588FG(2) of the *Corporations Act.* That defence is commonly described, in broad terms, as a “good faith” defence, although it has four different limbs and only one of those is concerned with good faith. Section 588FG(2) provides as follows:

**Transaction not voidable as against certain persons**

…

(2) A court is not to make under section 588FF an order materially prejudicing a right or interest of a person if the transaction is not an unfair loan to the company, or an unreasonable director-related transaction of the company, and it is proved that:

(a) the person became a party to the transaction in good faith; and

(b) at the time when the person became such a party:

(i) the person had no reasonable grounds for suspecting that the company was insolvent at that time or would become insolvent as mentioned in paragraph 588FC(b); and

(ii) a reasonable person in the person’s circumstances would have had no such grounds for so suspecting; and

(c) the person has provided valuable consideration under the transaction or has changed his, her or its position in reliance on the transaction.

#### The four limbs of s 588FG(2)

190 The test in s 588FG(2) has four limbs which must be satisfied. The liquidators made reference to the elements in the four limbs by reference to whether they involved “subjective” or “objective” requirements. In *Dean-Willcocks v Commissioner of Taxation* [2008] NSWSC 1113 [10], Barrett J explained of the second and third limbs that it is not helpful to attempt to characterise one inquiry as “subjective” and the other as “objective”. One reason for this is that the words “subjective” and “objective” are sometimes used in different ways. For instance, a test can be objective even if it focuses upon particular circumstances, or even particular knowledge, of a defendant. But some consider that such a test is subjective. The better approach is not to be distracted by labels that are not contained in the legislation.

191 The first limb, in s 588FG(2)(a), focuses upon “good faith” in how the person *became* a party to the transaction. The liquidators submitted that CSR had not satisfied this limb. In *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd* [2011] NSWCA 109; (2011) 81 NSWLR 47, 67 [154], Young JA (with whom Hodgson and Whealy JJA agreed on this point) said that, broadly speaking, a creditor will prima facie act in good faith where it receives the payment of a genuine debt, unless that prima facie position is displaced. I do not consider that Young JA was suggesting a reversal of the onus of proof. Rather, his Honour was observing only that the usual course in commerce was that creditors do not enter into transactions in bad faith.

192 There may be large questions about the precise content of “good faith” in s 588FG(2)(a). As I explained in *Mineralogy Pty Ltd v Sino Iron (No 6)* [2015] FCA 825 [1007], in different contexts the term “good faith” can mean different things. This is particularly so where the term is used in a particular statutory context. In this statutory context, the emphasis on matters of reasonableness in the later limbs of s 588FG(2) tends to emphasise that the content of good faith in the first limb is, in large part, directed towards how the corporation behaved based only upon its actual knowledge. The parties in this case treated the good faith limb in this way. It is convenient to follow that approach in this case, without the need to decide the issue.

193 The second limb, in s 588FG(2)(b)(i), focuses upon what the defendant actually knew and asks whether that actual knowledge provided reasonable grounds for suspicion of insolvency (putting to one side s 588FC). The liquidators did not focus on this limb. It need not be considered here.

194 The third limb, in s 588FG(2)(b)(ii) focuses upon what a reasonable person in the defendant’s circumstances would have known and asks whether that knowledge provided grounds to suspect insolvency. The reasonable person in this limb is the reasonable business person: *Cussen (as Liquidator of Akai Pty Ltd) v Commissioner of Taxation* [2004] NSWCA 383; (2004) 51 ACSR 530, 538 [31] (the Court). The concept of “suspecting” requires more than idle wondering. It is a positive feeling of actual apprehension or mistrust without sufficient evidence: *Queensland Bacon Pty Ltd v Rees* [1966] HCA 21; (1966) 115 CLR 266, 303 (Kitto J). The relevant suspicion must also be a suspicion of actual and existing insolvency, as distinct from impending or potential insolvency: *Sheahan v Fabienne Pty Ltd* [1999] SASC 335 [30] (the Court); *Dean-Willcocks v Commissioner of Taxation* [2008] NSWSC 1113 [13] (Barrett J); *Burness, In the matter of Denward Lane Pty Ltd (ACN 065 418 411) (In Liquidation)* [2009] FCA 893 [52] (Gordon J). As Kitto J explained in *Rees* (at 303) it involves:

something which in all the circumstances would create in the mind of a reasonable person in the position of the payee an actual apprehension or fear that the situation of the payer is in actual fact that which the sub-section describes - a mistrust of the payer’s ability to pay his debts as they become due and of the effect which acceptance of the payment would have as between the payee and the other creditors.

195 The liquidators submitted that the third limb of CSR’s defence was not satisfied.

196 The fourth limb, in s 588FG(2)(b), involves an assessment of whether valuable consideration was provided under the transaction or whether there was a change of position. In determining whether the change of position was in reliance upon the transaction there may be difficult questions concerning whether “in reliance upon” requires a “but for” test of causation or a test involving material contribution to decision making: for one view see E Bant, *The Change of Position Defence* (Hart Publishing, 2009) 31-49, 143-160. These questions do not arise here because the liquidators did not put the fourth limb in issue in this case.

197 Strictly, this defence does not need to be decided because I have concluded that the payments were not unfair preferences. But since the parties made detailed submissions on the elements of the defence I will express my conclusions on them. It suffices to say that I consider that the first limb was satisfied based upon my assessment of Mr Mulholland and (albeit with serious reservations) my assessment of Mr Sellick. But, if I had concluded that FPJ Group was insolvent then I would have rejected this defence on the basis that CSR did not establish that a reasonable person in the circumstances of CSR would have had no grounds to suspect that FPJ Group was insolvent.

#### The first limb dispute: good faith

198 The parties’ submissions on this limb focused upon the notion of good faith in a vacuum. The submissions tended to conflate the questions of good faith of CSR in *becoming* a party to the transaction with the question of good faith of CSR in receiving payment under a transaction to which it had already become a party. As I have already observed, there were no submissions made about the meaning of “transaction”.

199 Although I have approached Mr Sellick’s evidence with great caution, there are five reasons why I conclude that CSR, by Mr Sellick and Mr Mulholland, was acting in good faith. The first is that the liquidators’ submissions focused upon the wrong legal issue and when the correct question is asked, good faith is apparent. The legal question is whether CSR *became* a party to the transaction in good faith. It is not whether, having become a party, it received a payment in good faith in the performance of a part of a continuing business relationship, although good faith in the receipt can be relevant to the legal question. When the correct legal question is asked it is clear that apart from the last supply of goods on 21 May 2014, which appears to have occurred by error, CSR did not enter any of the transactions for any reason other than a continued business and trading relationship with FPJ Group.

200 The next four reasons reinforce this conclusion. Since the receipt of payments was part of a continued business relationship, and running account, they are relevant to the question of whether CSR continued to enter the transaction or transactions in good faith.

201 **First**,Mr Sellick produced a report for senior management each month which advised about the status of debt for customers who had not paid for more than 60 days. He provided reports for November 2013, January 2014, February 2014, March 2014, and April 2014. Each of these reports contained around 20 customers. Many customers were repeated. In March 2014, the number of customers of CSR who had exceeded 60 days for payment was more than 10% of its credit sales for that month. FPJ Group was not one of these customers. FPJ Group was not contained in any of those reports.

202 **Secondly**,in March 2012 Mr Sellick extended FPJ Group’s trading terms from 30 days from the end of the month plus seven days’ grace to 30 days from the end of the month plus 16 days’ grace. Those trading terms remained the same until the end of May 2014.

203 Although FPJ Group routinely paid its accounts after the *written* 30 day credit terms, this was common in the building industry. From the perspective of CSR, FPJ Group’s payments fell within the group of between 65% and 72% of customers who paid between 30 and 60 days. On average, CSR’s credit customers paid their invoices between 50 and 53 days.

204 The common nature of late payments in the building industry puts into perspective the delays by CSR. It is also noteworthy that the first alleged preference payment was only 8 days later than the 45 day period (including the days of grace). CSR’s internal credit records, which reveal the number of days that FPJ Group paid outside its credit terms, did not reveal any marked deterioration in timing of payments other than several days longer than usual in November 2013. That pattern can be seen in the table below:

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Month of invoices** | **Applicable credit limit** | **Applicable CSR internal risk code** | **Date of payments by FPJ Group** | **Amount of FPJ Group payments** | **Date due for payment by FPJ Group as per credit application** | **Days outside of CSR’s payment terms as per credit application** | **Date due for payment by FPJ Group as per CSR risk code** | **Days outside of CSR’s payment terms as per CSR risk code** |
| March 2013 | $160,000 | 12 | 23.05.13  23.05.13  23.05.13 | $3,991.30  $3,467.57  $20,122.14 | 30.04.14 | 23 days  23 days  23 days | 16.05.13 | 7 days  7 days  7 days |
| April 2013 | $160,000 | 12 | 21.06.13  21.06.13 | $17,684.80  $7,891.32 | 31.05.13 | 21 days  21 days | 16.06.13 | 5 days  5 days |
| May 2013 | $160,000 | 12 | 22.07.13  22.07.13  22.07.13 | $661.10  $7,091.50  $18,852.09 | 30.06.13 | 22 days  22 days  22 days | 16.07.13 | 6 days  6 days  6 days |
| June 2013 | $160,000 | 12 | 19.08.13  19.08.13  19.08.13 | $16,621.67  $1,743.95  $10,581.68 | 31.07.13 | 19 days  19 days  19 days | 16.08.13 | 3 days  3 days  3 days |
| July 2013 | $160,000 | 12 | 12.09.13  12.09.13  12.09.13 | $12,261.19  $671.18  $3,502.73 | 30.08.13 | 13 days  13 days  13 days | 16.09.13 | 0 days  0 days  0 days |
| August 2013 | $160,000 | 12 | 10.10.13  14.10.13  16.10.13  17.10.13 | $10,000.00  $20,065.53  $10,000.00  $10,000.00 | 30.09.13 | 10 days  14 days  16 days  17 days | 16.10.13 | 0 days  0 days  0 days  1 day |
| September 2013 | $160,000 | 12 | 19.11.13  22.11.13  25.11.13  26.11.13  28.11.13 | $15,938.94  $10,000.00  $5,000.00  $4,000.00  $6,000.00 | 31.10.13 | 19 days  22 days  25 days  26 days  28 days | 16.11.13 | 3 days  6 days  9 days  10 days  12 days |
| October 2013 | $160,000 | 12 | 09.12.13  12.12.13  13.12.13 | $10,800.32  $27,000.00  $10,000.00 | 30.11.13 | 9 days  12 days  13 days | 16.12.13 | 0 days  0 days  0 days |
| November 2013 | $160,000 | 12 | 22.01.14  30.01.14  31.01.14  31.01.14 | $5,770.01  $10,000.00  $3,000.00  $5,000.00 | 31.12.13 | 22 days  30 days  31 days  31 days | 16.01.14 | 6 days  14 days  15 days  15 days |
| December 2013 | $160,000 | 12 | 20.02.14  20.02.14 | $5,085.32  $16,000.00 | 31.01.14 | 20 days  20 days | 16.02.14 | 4 days  4 days |
| January 2014 | $160,000 | 12 | 13.03.14  18.03.14  20.03.14  21.03.14  24.03.14 | $6,555.44  $5,000.00  $7,000.00  $7,500.00  $7,500.00 | 02.03.14 | 11 days  16 days  18 days  19 days  22 days | 18.03.14 | 0 days  0 days  2 days  3 days  6 days |
| February 2014 | $125,000  (20.02.14) | 12 | 14.04.14  16.04.14  24.04.14  28.04.14  29.04.14  30.04.14 | $15,630.46  $5,000.00  $5,000.00  $5,000.00  $5,000.00  $14,000.00 | 31.03.14 | 14 days  16 days  24 days  28 days  29 days  30 days | 16.04.14 | 0 days  0 days  8 days  12 days  13 days  14 days |
| March 2014 | $125,000 | 12 | 07.05.14  07.05.14  07.05.14 | $18,465.68  $119.03  $6,928.41 | 30.04.14 | 7 days  7 days  7 days | 16.05.14 | 0 days  0 days  0 days |

205 **Thirdly**, Mr Sellick said that there were three matters that indicated to him that a customer was in serious financial difficulty. Those matters are as follows:

(1) when a customer is asked to pay but the customer responds saying that he or she is unable to pay and is not able to put a payment plan in place;

(2) when a customer’s telephone number is disconnected, emails bounce, or mail is returned; and

(3) when a payment plan is put in place with a customer who has not paid on time and the customer then fails to comply with that plan.

206 None of these matters was satisfied in relation to FPJ Group over the period of the alleged preference payments. I place little weight on the actual language used by Mr O’Toole in his emails to Mr Sellick. Although he occasionally used language such as “struggling to get money in” and referred on some occasions to “hoping” to obtain payment, this language was used in the context of explaining delays in payment which were common in the industry and, as Mr Mulholland said (ts 211), Mr O’Toole had frequently said that he had money coming in.

207 **Fourthly**, CSR’s treatment of FPJ Group’s credit limit does not reveal any basis for an inference of a lack of good faith or any actual suspicion of insolvency. CSR increased the credit limit for FPJ Group on a number of occasions between October 2010 and February 2014. Originally the credit limit was $20,000. On 12 October 2010 it was increased to $100,000. On 19 May 2011 it was increased to $140,000. On 6 June 2012 it was increased to $160,000.

208 On 20 February 2014, however, CSR reduced the credit limit of FPJ Group to $125,000. Mr Sellick’s explanation for this was that FPJ Group’s trading had reduced below the $160,000 limit. I do not accept this explanation. In cross-examination, Mr Sellick accepted that throughout the whole of 2013 the orders by FPJ Group had never reached even $50,000 (ts 150). Mr Sellick properly accepted that at the end of January 2014 he had expected that FPJ Group would go beyond the 60 day limit (which would lead to a stop being put on its account) (ts 150). Indeed, the email that Mr Sellick sent to Mr O’Toole on 28 January 2014 was the first time that Mr Sellick had ever said to Mr O’Toole that if FPJ Group exceeded 60 days then CSR would be unable to continue to supply FPJ Group. I infer that this was the real reason why Mr Sellick reduced the credit limit for FPJ Group to $125,000.

209 Although Mr Sellick anticipated that FPJ Group would go beyond the 60 day payment limit which was 15 days more than its trading terms, he only reduced the credit limit to $125,000. This credit limit was still more than double the size of FPJ Group’s orders from CSR. It reflected a concern by Mr Sellick that FPJ Group might fall into the most tardy 5% of customers for that month. As I have explained, the proportion of CSR’s customers who paid outside 60 days from December 2013 to July 2014 varied from 2%-10% with the usual proportion at around 5%. CSR knew, through Mr Sellick (ts 125), that some of these customers went into liquidation. Although, after anxious deliberation, I conclude that Mr Sellick did not make this assessment in relation to FPJ Group, as I explain below a reasonable person in his position would have done so.

#### The third limb dispute: lack of suspicion by a reasonable person in the circumstances

210 Although I accept that CSR was acting in good faith, I conclude that a reasonable person in the circumstances would have had sufficient knowledge to provide grounds to suspect insolvency at the time of all of the alleged preference payments apart from the first payment for four cumulative reasons. I reiterate, however, that a suspicion of insolvency is not the same as the proof of insolvency. In this case, the liquidators have not proved insolvency.

211 **First**, although CSR had extended the FPJ Group terms from 30 days to 45 days, the usual terms for the industry were payment within 30 days (from the end of the month). On those usual terms, FPJ Group had never paid within 30 days. FPJ Group had the worst payment record of Mr Mulholland’s clients in central Queensland (ts 212).

212 **Secondly**, a reasonable person in the position of CSR would have been aware, even if Mr Sellick was not, of the matters about which Mr Box gave evidence concerning the difficult economic conditions during 2013 and 2014 of the building industry in Rockhampton and Emerald (where it ought to have known one of FPJ Group’s major customers was based). As Mr Box explained, the decline in the mining boom meant that people had stopped buying houses. And as Mr Mulholland accepted (ts 212), there was a significant downturn from mid-2013.

213 **Thirdly**,CSR ought reasonably to have been aware that it was unlikely that FPJ Group had any “big jobs” or “major projects” from the end of 2013. Mr Mulholland could not recall precise details, and Mr Sellick was not aware of any major projects (ts 147: Mr Sellick; ts 213: Mr Mulholland), but a reasonable person in CSR’s position would have drawn the conclusion that it was unlikely that FPJ Group had any major projects at this time.

214 **Fourthly**,CSR was aware, through Mr Sellick, that only a small percentage of companies went beyond 60 days of credit (following the end of the month). As Mr Sellick was aware, some of those companies had gone into liquidation. By the end of January 2014, CSR expected, reasonably, that FPJ Group would exceed 60 days.

215 In light of all the matters above, CSR, acting reasonably, should have suspected insolvency at the end of January 2014.

## Issue 5: Were the payments part of a running account under s 588FA(3)?

216 The second “defence” relied upon by CSR was that the payments were part of a running account. Strictly, the running account in s 588FA(3) is not a defence. It is a requirement in the proof of an unfair preference. To recap, the subsection provides:

(3) Where:

(a) a transaction is, for commercial purposes, an integral part of a continuing business relationship (for example, a running account) between a company and a creditor of the company (including such a relationship to which other persons are parties); and

(b) in the course of the relationship, the level of the company's net indebtedness to the creditor is increased and reduced from time to time as the result of a series of transactions forming part of the relationship;

then:

(c) subsection (1) applies in relation to all the transactions forming part of the relationship as if they together constituted a single transaction; and

(d) the transaction referred to in paragraph (a) may only be taken to be an unfair preference given by the company to the creditor if, because of subsection (1) as applying because of paragraph (c) of this subsection, the single transaction referred to in the last-mentioned paragraph is taken to be such an unfair preference.

217 The running account was considered by the High Court of Australia in *Airservices Australia v Ferrier* [1996] HCA 54; (1996) 185 CLR 483. In that case, Dawson, Gaudron and McHugh JJ explained the rationale of the running account in the context of s 122 of the *Bankruptcy Act 1966* (Cth) (at 501-502, footnotes omitted):

If a payment is part of a wider transaction or a “running account” between the debtor and the creditor, the purpose for which the payment was made and received will usually determine whether the payment has the effect of giving the creditor a preference, priority or advantage over other creditors. If the sole purpose of the payment is to discharge an existing debt, the effect of the payment is to give the creditor a preference over other creditors unless the debtor is able to pay all of his or her debts as they fall due. But if the purpose of the payment is to induce the creditor to provide further goods or services as well as to discharge an existing indebtedness, the payment will not be a preference unless the payment exceeds the value of the goods or services acquired. In such a case a court, exercising jurisdiction under s 122 of the *Bankruptcy Act*, looks to the ultimate effect of the transaction. Whether the payment is or is not a preference has to be “decided not by considering its immediate effect only but by considering what effect it ultimately produced in fact”.

218 On the face of things, each of the alleged unfair preference payments was, for commercial purposes, an integral part of a continuing business relationship between FPJ Group and CSR, and that in the course of the relationship, the level of FPJ Group’s net indebtedness to CSR was increased and reduced from time to time as a result of a series of transactions forming part of the relationship. However, the liquidators submitted that CSR had notice of FPJ Group’s insolvency and that this notice effectively destroyed the continuing business relationship.

219 CSR relied on the evidence of Mr Sellick that $43,738.86 remained due and owing from FPJ Group to CSR on 18 July 2014 as part of the running account. Mr Sellick’s evidence was also that during the period from 19 January and 18 July 2014 the highest amount owing was $95,444.50. Since there allegedly remained $43,738.86 owing, CSR relied upon the running account to submit that the liquidators could only claim $51,705.64.

220 Apart from quoting the principle of a running account, neither the liquidators nor CSR referred to any authority on s 588FA(3). The reason for this may have been that the liquidators’ submissions were narrowly confined. The liquidators submitted that CSR had notice of FPI Group’s insolvency at the time of the alleged preference payments so that CSR was no longer making payments while “looking forwards” to the provision of continuing services. This submission conflated issues of notice and the issue of whether one purpose of the payments was inducing further supply. Although notice might be one circumstance to consider, the issue requires consideration of all the circumstances to determine whether payments are made in the mutual expectation that the creditor will continue to supply the debtor. As Peek J said in *Clifton v CSR Building Products Pty Ltd* [2011] SASC 103 [68], “it is necessary to look at the particular circumstances from which it may be inferred since usually there will be no express statement that a payment is being made in the expectation that the supplier will continue to supply”.

221 In *Sydney Appliances Pty Ltd (in liq) v Eurolinx Pty Ltd* [2001] NSWSC 230 [148], Santow J explained some “essential prerequisites” for the defence in s 588FA(3), separating notice from the purpose of the payments:

First, there must be no cessation of that mutual assumption of payment and reciprocal supply throughout the relevant period. Second, those payments must continue to have at least one operative, mutual purpose, namely inducing further supply. I would add that such purpose must not come to be subordinated to a predominant purpose of recovering past indebtedness. As the decision in *Airservices Australia* makes clear … knowledge or even actual suspicion, though it be such as to negate the good faith defence, does not of itself preclude reliance upon the running account defence for a payment so received.

222 It has subsequently been reiterated that a suspicion of insolvency or reasonable grounds to suspect insolvency might not destroy a continuing business relationship: *Clifton v CSR Building Products* [69]-[70] (Peek J); *Carello as Liquidator of Perrinepod Pty Ltd (In Liq) v Perrine Architecture Pty Ltd* [2016] WASC 145 [253]-[254] (Chaney J). As Chaney J observed in *Carello* [251], by reference to the decision of Master Burley in *Olifent v Australian Wine Industries Pty Ltd* (1996) 19 ACSR 285, 293, circumstances that might destroy the continuing business relationship could be where payments were not received in good faith, or were not made in the ordinary course of business, or were made when the parties knew the company to be insolvent.

223 Apart from the exception to which I refer immediately below, and for the reasons above at [201]-[209], I am satisfied that FPJ Group’s payments throughout November 2013 until 20 May 2014 continued to be made for at least one operative purpose being to induce further supply by CSR. Although at the end of January 2014 Mr Sellick thought that a stop might be put on FPJ Group’s account until its invoice was paid, he did not expect that their trading relationship would cease. In any event, no stop was ever put on the account. Until about 20 May 2014, the parties mutually assumed that there would be a continuance of their relationship as buyer and seller.

224 Ultimately, any adjudication of this point would have required further submissions from counsel concerning the evidence relating to the alleged $43,738.86 which CSR said was still owed to it by FPJ Group on 18 July 2014. CSR tendered, through annexures to Mr Sellick’s affidavit, numerous purchase orders, delivery dockets, picking slips, tax invoices and credit notes. This evidence was in support of the alleged debt of $43,738.86. But no submissions were made about which goods related to which part of the debt or when those goods were supplied, and when the debt was incurred.

225 The reason why submissions on this point would have been important is that the exception in s 553C(2) applies at the time the debt is incurred. Some of the debt of $43,738.86 was incurred when CSR was plainly aware that FPJ Group was insolvent. As I have explained, on 20 May 2014 Mr O’Toole met with Mr Mulholland and told Mr Mulholland that staff at FPJ Group had been informed that it would be closing. Mr Mulholland told Mr Sellick and Mr Sellick placed a manual stop on FPJ Group’s account. Yet goods were nevertheless dispatched on 21 May 2014. The cost of those goods was included in the claim by CSR for a set-off. It is very strongly arguable that these amounts of the debt, if included in the $43,738.86, should have been excluded because at that stage FPJ Group was no longer incurring the debt as part of a relationship of continuing supply.

## Issue 6: Does CSR have a set-off under s 553C?

226 CSR relied upon s 553C of the *Corporations Act* as follows:

**Insolvent companies--mutual credit and set-off**

(1) Subject to subsection (2), where there have been mutual credits, mutual debts or other mutual dealings between an insolvent company that is being wound up and a person who wants to have a debt or claim admitted against the company:

(a) an account is to be taken of what is due from the one party to the other in respect of those mutual dealings; and

(b) the sum due from the one party is to be set off against any sum due from the other party; and

(c) only the balance of the account is admissible to proof against the company, or is payable to the company, as the case may be.

(2) A person is not entitled under this section to claim the benefit of a set-off if, at the time of giving credit to the company, or at the time of receiving credit from the company, the person had notice of the fact that the company was insolvent.

#### The cases that the liquidators submitted were wrongly decided

227 The liquidators denied that CSR was entitled to a set-off. Essentially, the submission of the liquidators was that numerous decisions which had held or suggested the contrary were either in error or were plainly wrong. The first of these cases is the decision of the Federal Court in 1997 in *Re Parker* (1997) 80 FCR 1. The second of these cases is the decision of the New South Wales Court of Appeal in *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia* [2011] NSWCA 109; (2011) 81 NSWLR 47. The third of these cases is another decision of the Federal Court in *Smith v Boné in the matter of ACN 002 864 002 Pty Ltd (in liq)* [2015] FCA 319. A fourth case, not referred to by the liquidators, but which the liquidators’ submissions probably meant was also wrongly decided is the decision of the New South Wales Supreme Court in *Hall v Poolman* [2007] NSWSC 1330; (2007) 65 ACSR 123. A fifth case, again not referred to by the liquidators but also probably inconsistent with the liquidators’ submissions, is *Shirlaw v Lewis* (1993) 10 ACSR 288. A sixth case, also not referred to by the liquidators, but again also probably inconsistent with some of their submissions is *JLF Bakeries Pty Ltd (in liq) v Baker’s Delight Holdings Ltd* [2007] NSWSC 894; (2007) 64 ACSR 633.

228 This line of authority began in *Re Parker* (1997) 80 FCR 1, where Mansfield J allowed a set-off under s 553C to a claim for recovery of a payment from a holding company under s 588W, which was based on insolvent trading under s 588V.

229 The conclusion in *Re Parker* was considered in the context of s 588FF in *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia* [2011] NSWCA 109; (2011) 81 NSWLR 47. In that case, Young JA (with whom Hodgson and Whealy JJA agreed) held that two payments made by Buzzle to Apple Computer were uncommercial transactions. Strictly the set-off defence did not need to be considered because the “good faith” defence in s 588FG(2) applied. However Young JA observed that senior counsel for Buzzle had not ultimately submitted that the court should depart from *Re Parker* (at 80 [276])*.* Instead, he had submitted that *Re Parker* should be confined to allowing a set-off for a claim for recovery under s 588W, but not extended to recovery under s 588FF. This submission was not accepted (at 80-81 [277]-[278]). Young JA assumed that *Re Parker* was correctly decided and, on that basis, refused to distinguish a claim for recovery of payments made in insolvent trading under s 588W from claims for recovery under s 588FF based on commercial transactions.

230 The conclusion in *Re Parker* was again applied in the Federal Court by Gleeson J in *Smith v Boné in the matter of ACN 002 864 002 Pty Ltd (in liq)* [2015] FCA 319 [420].

231 These three cases (*Re Parker, Buzzle Operations,* and *Smith v Boné*) were the only cases mentioned by the liquidators. The liquidators did not make any detailed submissions about the reasoning in any of these cases. Initially the liquidators just sought to distinguish them on the basis that they involved different facts or because the provision which created a preference was different (even if, in the latter two cases, the provision which empowered the unwinding of the transaction – s 588FF – was the same). Those submissions were rightly abandoned in oral argument: see also *Cashflow Finance Pty Ltd (in liq) v Westpac Banking Corp* [1999] NSWSC 671 [574] (Einstein J).

#### The submissions concerning why the cases were wrongly decided

232 The liquidators then made two submissions of principle for why all the authorities that they cited on this point should be rejected. It suffices to explain why I reject the two submissions of principle that were made by the liquidators before explaining why it is both unnecessary and undesirable to reach any conclusions on the question of whether the line of authority against the liquidators is wrongly decided.

233 The first submission of principle by counsel for the liquidators in support of the suggestion that all of these cases were wrongly decided was that if a set-off were to be allowed, then to set-off a liability in respect of the preference payments against other non-preference debts would lead “to the peculiar result that a creditor who is paid [its] entire debt by preference payments will be disadvantaged as compared [with] a creditor who is paid only part of [its] debt by preference payments”. In other words, counsel submitted that it would be a “peculiar” conclusion if a creditor who obtains a larger amount of unfair preference payments should have to make a larger payment back to the company. That conclusion is not peculiar. It is the plain effect of the legislative provisions and the legislative policy.

234 Another submission by the liquidators was that it would be “perverse” if creditors could “happily accept preferential payments knowing that those payments will be treated as 100c in the $ for the purposes of a set-off for the balance of the outstanding amounts”. Such a situation involving a “happy” receipt from a company known to be insolvent might, indeed, be perverse. However, the short answer to this submission is that s 553C(2) does not permit such happiness.

235 There are, however, powerful contrary arguments that might have been made to suggest that a set-off is not available against a liquidator’s claim to recover preference payments. Many of these arguments are made in Dr Derham’s book: Derham R, *Derham on the Law of Set-off* (4th ed, Oxford University Press, 2010) 537-547. Those arguments were expanded in a recent article by Dr Derham: Derham, R “Set-off Against Statutory Avoidance and Insolvent Trading Claims in Company Liquidation” (2015) 89 *Australian Law Journal* 459.

236 There are numerous reasons why I do not consider it appropriate to assess these arguments concerning whether a set-off should be available in this case. The first reason is that I do not accept the liquidators’ brief submissions of principle and the liquidators did not address any of Dr Derham’s arguments. The second reason is that it is unnecessary to determine the question of set-off because of the conclusions I have reached in relation to the lack of proof of insolvency and the secured nature of the debts. It suffices in this part of my reasons to indicate a number of additional matters that would need to have been addressed even beyond those matters addressed in Dr Derham’s comprehensive writings on this topic.

#### Outflanking of a running account?

237 The first additional matter which was not addressed is the question of whether a set-off claim can be used to outflank the statutory running account in s 588FA(3). This additional matter arises even if, which I do not decide, s 553C is not excluded by a claim for relief under s 588FF for an unfair preference (where such exclusion would be on the basis that Part 5.7B of the *Corporations Act* was intended to codify the law relating to unfair preferences). The additional question is whether s 553C could be said to have been excluded only to the extent that it involved an attempt to reframe a running account as a set-off.

238 A number of authorities have described the effect of s 588FA(3) as codifying the law of preferences in relation to the running account for the purposes of s 588FA: see *Sydney Appliances Pty Ltd (in liq) v Eurolinx Pty Ltd* [2001] NSWSC 230 [138]-[139] (Santow J); *VR Dye & Co v Peninsula Hotels Pty Ltd (in liq)* [1993] 3 VR 201 [27] (Ormiston JA); *Sutherland v Lofthouse* [2007] VSCA 197; (2007) 214 FLR 157, 166-167 [34] (Nettle JA); *Lopez (In his capacity as liquidator of Swan Concrete Products Pty Ltd (in liq)) v Harvey* [2015] WASC 292 [25] (Chaney J).

239 As s 588FA(3) was a provision intended to codify the principles of a running account, there may be questions whether a set-off claim could be made where the debts that are sought to be set-off are those that might otherwise have fallen within a running account. It may be that there is no inconsistency because although the principles have sometimes been stated in similar terms (see *Sutherland v Liquor Administration Board* (1997) 15 ACLC 875, 211 (Young J)) the doctrine of set-off remains conceptually distinct from the running account so that the codification of the running account would not be outflanked by permitting a concurrent claim for set-off. But before I were to determine whether s 553C applied to a claim under s 588FF based upon an unfair preference under s 588FA, it would have been necessary for me to hear submissions about the history of s 588FA(3) and its relationship with s 553C of the *Corporations Act*. I did not call for further submissions in light of the conclusions that I reached about the liquidators’ failure to prove insolvency and the nature of the debt as secured.

#### Unaddressed issues in relation to notice

240 The second submission by the liquidators was that the exception in s 553C(2) applied because at the time of each of the alleged preference payments CSR had notice of the fact that FPJ Group was insolvent. The concept of “notice” in law is different from the concept of “knowledge”. In relation to liability of those who are accessories to a breach of trust in equity, for example, a taxonomy of notice is commonly used which differentiates five different degrees of notice: *Farah Constructions Pty Ltd v Say–Dee Pty Ltd* [2007] HCA 22; (2007) 230 CLR 89, 163 [174], referring to *Baden v Société Générale pour Favoriser le Dévelopment du Commerce et de l’Industrie en France SA* [1992] 4 All ER 161, 235, 242-243.

241 In this case, the liquidators accepted that the test for “notice” in s 553C(2) was that which had been applied in *Jetaway Logistics Pty Ltd v Deputy Commissioner of Taxation* [2009] VSCA 319; (2009) 26 VR 657. That was the first four levels of knowledge from *Baden.* In *Jetaway Logistics*, the Victorian Court of Appeal explained (at 662 [22]) that:

What is required is proof of facts known to the creditor which warranted the conclusion of insolvency. Since “grounds for suspecting” insolvency will not suffice, it is not enough that insolvency is a possible inference from the known facts. Whether it must be the only reasonable inference open is a question we need not decide.

242 The issue of notice was thus treated as whether an inference could be drawn on the balance of probabilities that FPJ Group knew of circumstances which would have indicated the fact of insolvency to an honest and reasonable person. It is not necessary in this case to explore that assumption. It suffices to repeat that it is not possible for this Court to draw the inference, on the evidence before it, that FPJ Group was insolvent on 21 November 2013 or before late May 2014. Likewise, there are insufficient facts from which any inference could be drawn that CSR knew of circumstances which would have indicated the fact (which has not been proved) that FPJ Group was insolvent on that date or at any time before late May 2014.

243 However, as I have explained in relation to the running account, any adjudication of this point would have required further submissions from counsel concerning the alleged $43,738.86 which CSR said was owed to it by FPJ Group on 18 July 2014. It is not currently possible simply to accept that as the amount of set-off when, on any view, the cost of the goods dispatched on 21 May 2014 would fall within the exception in s 553(2) of the *Corporations Act*.

#### The “contingent debt” question

244 Another question concerning set-off which was not addressed in detail in submissions but which would have been necessary to address before a conclusion was reached is the application of s 553C(1)(a) of the *Corporations Act*.

245 Under s 553C(1)(a) it is necessary to identify whether a potential liability to repay a voidable preference falls within the “account .. to be taken of what is due from the one party to the other in respect of [their] mutual dealings”. There may be questions concerning whether it is possible to attach the label “contingent debt” to a transaction that is voidable in order to characterise it as an amount which is “due”: compare the different answers given to related questions in *In re Nortel GmbH (in administration) and related companies* [2013] UKSC 52;[2014] AC 209 and *Foots v Southern Cross Mine Management Pty Ltd* [2007] HCA 56; (2007) 234 CLR 54. In turn, those questions might be affected by whether the power of the court to avoid a transaction under s 588FF is discretionary and, if so, whether s 553C(1)(a), properly construed, creates an existing debt which is due despite the necessity for the later exercise of a discretion by the Court.

246 There are also related questions concerning the nature of any discretion in s 588FF including whether there is any discretion which permits the Court not to make an order within that section once the power has been enlivened. On the one hand, it is necessary to consider cases such as *BP Australia Ltd v Brown* [2003] NSWCA 216; (2003) 58 NSWLR 322, 352 [157], 354 [171], 357 [187] (Spigelman CJ); *Sheahan Pty Ltd v Murdock & Gediz Pty Ltd* [2008] SADC 5 [59], [61]-[62] (Tilmouth J); and *New Cap Reinsurance Corporation Ltd v A E Grant* [2009] NSWSC 662; (2009) 72 ACSR 638, 649 [59] (Barrett J). On the other hand there are potentially contrary authorities *Cashflow Finance Pty Ltd (in liq) v Westpac Banking Corp* [1999] NSWSC 671 [569]-[570] (Einstein J); *Cussen v Sultan* [2009] NSWSC 1114; (2009) 74 ACSR 496, 503-505 [25]-[30] (Nicholas J); and *Kazar v Kargarian* [2010] FCA 1381; (2010) 81 ACSR 158, 171 [28] (Flick J). The matter was not decided in *Buzzle* at 79 [258]-[261] (Young JA). See also the discussion in *Fortress Credit Corporation (Australia) II Pty Ltd* [2015] HCA 10; (2015) 254 CLR 489, 505-506 [24] (the Court). The absence of submissions on this point or on these cases is a further reason not to decide the larger issue concerning set-off.

## Conclusion

247 I dismiss the liquidators’ claims to recover $153,554 of payments on the basis that the payments were unfair preferences under s 588FE of the *Corporations Act.* The liquidators failed to prove that FPJ Group was insolvent. Further, all of the $153,554 was secured. No payment was an unfair preference.

248 These proceedings also involved a number of difficult legal issues. Submissions evolved during the course of trial. In closing submissions they were still evolving. There remained a number of matters which were not addressed, particularly in relation to the set-off claim. In circumstances in which (i) the liquidators’ claims fail for two significant reasons, (ii) a set-off would only have been around $40,000, and (iii) the legal fees had already exceeded the total claim of $153,554, I did not call upon the parties to make further submissions on any of these matters.

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| I certify that the preceding two hundred and forty eight (248) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Edelman. |

Associate:

Dated: 13 May 2016