Equity Division
Supreme Court
New South Wales

Case Name:	**In the matter of Force Corp Pty Ltd (in liq)**
Medium Neutral Citation:	**[2020] NSWSC 1842**
Hearing Date(s):	24 November 2020
Date of Orders:	17 December 2020
Date of Decision:	17 December 2020
Jurisdiction:	Equity – Corporations List
Before:	Gleeson J
Decision:	Directions given to liquidators in relation to proposed distributions to priority creditors in the liquidation of Force Corp Pty Ltd (in liq): see [133]
Catchwords:	CORPORATIONS – winding up – where company in liquidation – where assets available in liquidation sufficient to declare dividend to priority creditors – application by liquidators for directions concerning proposed distributions to priority creditors – Insolvency Practice Schedule (Corporations), *Corporations Act 2001* (Cth), Sch 2 – *Corporations Act* s 556(1) CORPORATIONS – where secured creditor advanced moneys to administrators – whether administrators entitled to indemnity for monies borrowed – *Corporations Act* ss 443A(1) and 443D – whether administrators liability to the secured creditor is a priority claim – *Corporations Act* s 556(1)(c) CORPORATIONS – where receivers made payments to former employees after commencement of winding up – whether secured creditor entitled to be subrogated to priority position of employee creditors – *Corporations Act* s 556(1)(e) – where receivers failed to pay amounts owing to other employees under s 556(1)(e) – *Corporations Act*, s 433(3) – where secured creditor acknowledged liability to company for amounts not paid by receivers to other employee creditors – whether insolvency set-off available –

Corporations Act, s 553C(1) – whether secured creditor had notice of fact of insolvency at time of receiving credit from the company – *Corporations Act*, s 553C(2) – whether equitable set-off available as alternative to insolvency set-off

EQUITY – whether rule in *Cherry v Boultbee* available as alternative to insolvency set-off

CORPORATIONS – where creditor made payment on account of employees' wages at the direction of the company – whether creditor entitled to priority for payment – *Corporations Act* s 560 and s 556(1)(e)

Legislation Cited:

Bankruptcy Act 1966 (Cth), s 86
Companies Act 1961 (NSW), s 292(1)(d)
Corporations Act 2001 (Cth), ss 51C, 79, 433, 436C, 439A, 439C, 443A, 443D, 479, 511, 513B, 513C, 553C, 556, 560, 561, 591, 1317E, Sch 2
Insolvency Practice Schedule (Corporations), ss 5-15, 90-15
Personal Property Securities Act 2009 (Cth), ss 9, 10, 51, 51C, 304, 340

Cases Cited:

Aged Care Services Pty Ltd v Kanning Services Pty Ltd (2013) 86 NSWLR 174; [2013] NSWCA 393
Australian Financial Services Leasing Pty Ltd v Hills Industries Ltd (2014) 253 CLR 260; [2014] HCA 14
Banque Financiere de la Cite v Parc (Battersea) Ltd [1999] 1 AC 221
Blakely, In the matter of Akron Roads Pty Ltd (in liq) [2020] FCA 1378
Bofinger v Kingsway Group Limited (2009) 239 CLR 269; [2009] HCA 94
Bryant, in the matter of Gunns Limited (in Liq) (receivers and managers appointed) v Bluewood Industries Pty Ltd [2020] FCA 714
Burness v Supaproducts Pty Ltd [2009] FCA 893; (2009) 259 ALR 33
Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd (2011) 81 NSWLR 47; [2011] NSWCA 109
Calzaturuficio Zenith Pty Ltd (in liq) v NSW Leather & Trading Co Pty Ltd; Victorian Leather Co Pty Ltd [1970] VR 605
Cherry v Boultbee [1839] Eng R 1099; (1839) 41 ER 171
CMI Industrial Pty Ltd (in liq), Re: Byrnes v CMI Ltd [2016] 1Qd R 241; [2015] QSC 96
Community Development Pty Ltd v Engwirda

Construction Co (1996) 120 CLR 455
Coventry v Charter Pacific Corp Ltd (2005) 227 CLR 234; [2005] HCA 67
David Securities Pty Ltd v Commonwealth Bank of Australia (1992) 175 CLR 353; [1992] HCA 48
Divitkos, in the matter of XDVD Pty Ltd (in liq) [2014] FCA 696; (2014) 223 FCR 409
Façade Treatment Engineering Pty Ltd v Multiplex Constructions Pty Ltd [2016] VSCA 247; 116 ACSR 493
Federal Commissioner of Taxation v Gosstray [1986] VR 876
GM & MA Pearce & Co Pty Ltd v RGM Australia Pty Ltd [1990] 4 VR 888
Grapecorp Management Pty Ltd (in liq) v Grape Exchange Management Euston Pty Ltd (2012) 265 FLR 33; [2012] VSC 112
Great Southern Ltd (Recs and Mgrs Appted) (in liq), Re ex parte Thackaray [2012] WASC 59; (2012) 260 FLR 362
Gye v McIntyre (1991) 171 CLR 609; [1991] HCA 60
Hall v Poolman (2007) NSWSC 1330; (2007) 65 ACSR 123
Hamersley Iron Pty Ltd v Forge Group Power Pty Ltd (in Liquidation) (Receivers and Managers Appointed) (2018) 53 WAR 325; [2018] WASCA 163
Hawes v Dean [2014] NSWCA 380
Highland v Exception Holdings Pty Ltd (in liq) [2006] NSWCA 318; (2007) 60 ACSR 223
Hiley v People's Prudential Assurance Co Ltd (in liq) (1938) 60 CLR 468; [1938] HCA 40
Hill v Ziymack (1908) 7 CLR 352 at 361; [1908] HCA 13
HP Mercantile Pty Ltd v Dierickx (2013) 306 ALR 53; [2013] NSWCA 479
Inland Revenue Commissioners v Goldblatt [1972] Ch 498; [1972] 2 All ER 202
Jetaway Logistics Pty Ltd v Deputy Commissioner of Taxation [2009] VSCA 319; (2009) 76 ACSR 404
JLF Bakeries Pty Ltd v Baker's Delight Holdings Ltd (2007) 64 ACSR 633; [2007] NSWSC 894
Jones (Liquidator) v Matrix Partners Pty Ltd, in the matter of Killarnee Civil & Concrete Contractors Pty Ltd (in liq) (2018) 260 FCR 310; [2018] FCAFC 40
Kirman v RWE Robinson and Sons Pty Ltd (in liq), in the matter of RWE Robinson and Sons Pty Ltd (in liq) [2019] FCA 372
Korda v Silk Chime Pty Ltd [2010] WASC 155; (2010) 243 FLR 269
Lombe v Wagga Leagues Club Limited [2006]

NSWSC 3
NA Kratzmann Pty Ltd v Tucker, Liquidator of Reid Murray Developments (Qld) Pty Ltd (No 2) (1968) 123 CLR 295; [1968] HCA 44
Old Style Confections Pty Ltd v Microbyte Investments Pty Ltd (In liq) (1995) 2 VR 457
Painter v Charles Whiting & Chambers Ltd (1932) 4 ABC 203
Re a Debtor [1927] 1 Ch 410; Re Clements; Ex parte Trustee; Goldsbrough Mort & Co Ltd (Respondent) (1931) 7 ABC 255;
Re Anglican Development Fund Diocese of Bathurst (receivers & managers appointed) [2015] NSWSC 44; (2015) 33 ACLC 15-010
Re Ansett Australia Ltd (Admins Apptd) and Korda [2002] FCA 90; (2002) 40 ACSR 433
Re Australian Institute of Professional Education Pty Ltd (in liq) [2018] FCA 780
Re Australian Institute of Professional Education Pty Limited (In Liquidation) (2018) 334 FLR 401; [2018] NSWSC 1028
Re Buchanan Enterprises Pty Ltd (No 2) (1982) 7 ACLR 407
Re Clements; Ex parte Trustee; Goldsbrough Mort & Co Ltd (Respondent) (1931) 7 ABC 255
Re Courtenay House Capital Trading Group Pty Ltd (in liquidation) [2002] NSWSC 780
Re Dalma (No 1) Pty Ltd (in liq) [2013] NSWSC 1335; (2013) 279 FLR 80
Re G B Nathan & Co Pty Ltd (in liq) (1991) 24 NSWLR 674
Re Hawden Property Group Pty Ltd (in liq) (2018) 125 ACSR 355; [2018] NSWSC 481
Re M F Global Australia Ltd (in liq) [2012] NSWSC 994; (2012) 267 FLR 27
Re Parker (1997) 80 FCR 1
Re PrimeSpace Property Investment Limited (in liq) [2018] NSWSC 919
Re RCR Tomlinson Ltd (administrators appointed) [2020] NSWSC 735
Re Smith; Ex parte Trustee; J Bird Pty Ltd and Tully (Respondents) (1933) 6 ABC 49
Saker, in the Matter of Great Southern Ltd [2014] FCA 771
Salomon v A Salomon & Co Ltd [1897] AC 22
Sanderson v Classic Car Insurances Pty Ltd (1985) 10 ACLR 115
Shirlaw v Lewis (1993) 10 ACSR 288
Smith (in his capacity as liquidator of ACN 002 864 002 Pty Ltd (in liq) (formerly known as Petrolink Pty

	Ltd) v Boné [2015] FCA 319 Stein v Blake [1995] 1 AC 243 Stein v Saywell (1969) 121 CLR 529 Steinberg v Herbert (1988) 14 ACLR 80 Stone v Melrose Cranes & Rigging Pty Ltd, in the matter of Cardinal Project Services Pty Ltd (in liq) (No 2) [2018] FCA 530; (2018) 125 ACSR 406 Victorian Leather Co Pty Ltd [1970] VR 605 Western (Liquidator), In the matter of 7 Steel Distribution Pty Limited (in liq) [2015] FCA 742 Walley, In the matter of Poles & Underground Pty Ltd (Admin Apptd) [2017] FCA 486 Westminster Corporation v Haste [1950] Ch 442; [1950] 2 All ER 65 Whitton v ACN 003 266 886 Pty Ltd (Controller Appointed) (In Liq) (1996) 42 NSWLR 123 Wollongong Coal Ltd v Gujarat NRE India Pty Ltd [2019] NSWCA 135
Texts Cited:	R Derham, *Derham on The Law of Set-Off*, (3rd ed., Oxford University Press, 2003) R Derham, “Set-off against statutory avoidance and insolvent trading claims in company liquidation” (2015) 89 ALJ 459 C Mitchell, *The Law of Subrogation* (Clarendon Press, Oxford, 1994)
Category:	Principal judgment
Parties:	David Lombe and Vaughan Neil Strawbridge as liquidators of Force Corp Pty Ltd (in liq) (First plaintiff) Force Corp Pty Ltd (in liq) (Second plaintiff) Lease Collateral Pty Ltd (Defendant)
Representation:	Counsel: D Krochmalik (Plaintiffs) C Bannan (Defendant) Solicitors: HWL Ebsworth Lawyers (Plaintiffs) Corrs Chambers Westgarth (Defendant)
File Number(s):	2020/234920
Publication Restriction:	

JUDGMENT

1 **GLEESON J:** Application is made by David John Frank Lombe and Vaughan Neil Strawbridge, the liquidators of Force Corp Pty Ltd (in liq) (Force Corp), for directions from the Court pursuant to s 90-15 of the Insolvency Practice Schedule (Corporations), being Sch 2 to the *Corporations Act 2001* (Cth), concerning distributions to priority creditors in the winding up under s 556(1) of the *Corporations Act*.

2 Mr Lombe and Mr Strawbridge were initially appointed administrators of Force Corp on 13 July 2015 by a secured creditor, Lease Collateral Pty Ltd (Lease Collateral) pursuant to s 436C. They became the liquidators of Force Corp on 23 November 2015, upon the creditors resolving that the company be wound up pursuant to s 439C(c) of the *Corporations Act*: s 446A(1)(a).

3 Also on 13 July 2015, another secured creditor, Recfin Nominees Pty Ltd (Recfin), appointed Christopher Clarke Hill and Brett Stephen Lord as the receivers and managers of the assets and undertaking of Force Corp pursuant to its rights under the security it held. Mr Lord subsequently retired as one of the receivers on 21 February 2017. Mr Hill retired and ceased to act as the receiver upon the finalisation of the receivership on 9 May 2019.

The directions sought

4 The liquidators have made recoveries in the winding up of Force Corp in excess of $2.3 million, sufficient to declare a dividend to priority creditors falling within subsections 556(1)(c), 556(1)(e) and 556(1)(g) of the *Corporations Act*. Other than the asserted claim by Lease Collateral to priority under s 556(1)(c) and (e), the liquidator has formed the view that the only other priority creditors entitled to a dividend by reason of claims falling within those subsections are:

(1) the Commonwealth (through the Attorney-General's Department administrating the Fair Entitlements Guarantee Scheme (FEG)) by

reason of its statutory right of subrogation in respect of monies paid to former employees of Force Corp on account of their employee entitlements; and

(2) certain other former employees of Force Corp on account of outstanding employee entitlements; and

(3) the Deputy Commissioner of Taxation (ATO) on account of superannuation (including with respect to the superannuation guarantee charge and superannuation on monies paid in lieu of notice).

5 The directions sought by the liquidators relate to four questions. The first concerns whether advances made by Lease Collateral to the administrators should be treated as a loan to the administrators for which they are entitled to be indemnified from the assets of Force Corp pursuant to s 443D(a) or 443D(a)(a) of the *Corporations Act*, such that the debt to Lease Collateral falls within s 556(1)(c). This is referred to as the funding on appointment issue.

6 The second concerns the nature of payments made by the receivers appointed to Force Corp to its employees with respect to wages and superannuation entitlements, and whether Lease Collateral is entitled to be subrogated to the position of employees with respect to claims that fall within s 556(1)(e). This is referred to as the subrogation issue.

7 The third concerns the consequences of the receivers' failure to pay from Force Corp's circulating assets the balance of employee wages and superannuation entitlements, and whether Lease Collateral's potential ancillary or restitutionary liability to Force Corp permits the amount not paid by the receivers from the circulating assets to be set off against the amount otherwise payable to Lease Collateral pursuant to s 556(1)(e). Initially, the liquidators relied upon insolvency set-off under s 553C(1) of the *Corporations Act*. After the Court raised the possible application of the rule in *Cherry v Boultbee*, the liquidators embraced this as an alternative analysis. In addition, in submissions filed after the hearing, the liquidators also relied upon

equitable set-off as an alternative to insolvency set-off. This is referred to as the offsetting claim issue.

8 The fourth concerns a payment made by Lease Collateral, at the direction of Force Corp, on account of employees' wages and whether the payment falls within s 560 of the *Corporations Act*, and has the priority given under s 556(1)(e). This is referred to as the LeasePLUS payment issue.

9 The financial outcome of the directions sought by the liquidators for creditors having priority under s 556(1)(c), (e) and (g), is set out in the following table which is reproduced from Mr Lombe's affidavit:

	Amount ($)
Estimated funds available for eligible unsecured priority creditors and claimants	2,322,099
S 556(1)(c) indemnity for Administrators' fees and expenses	(315,343)
• Lease Collateral Indemnity Claim	
Estimated s 556(1)(c) creditor claims	(315,343)
Balance available after distribution of s 556(1)(c) creditor claims	**2,006,756**
S 556(1)(e) wages and superannuation claims	
AGD (FEG) claim (for wages)	(40,138)
Lease Collateral claim:	
• LeasePlus Payment: $51,143 plus	
• Total Wages Payments after set-off: (309,952)	(361,095)
($856,515 for the Total Wages Payments less $546,563 for amounts not paid out of circulating assets in breach of s 433(3)(c))	
Australian Taxation Office (for superannuation)	(826,702)
Residual employee claims (wages $8,484 and superannuation $12,612)	(21,096)
Estimated s 556(1)(e) creditor claims	**(1,249,031)**
Balance available after distribution of s 556(1)(e)	**757,725**
S 556(1)(g) leave entitlement claims	
AGD (FEG) claim (annual leave and leave loading $1,016,853 and long service leave $656,350)	(1,673,203)
Residual employee claims (annual leave, leave loading and long service leave)	(268,769)
Sub-total: s 556(1)(g) creditor claims	**(1,941,972)**
Estimated distribution for s 556(1)(g) leave entitlement claims c/$	**0.3902**

10 Three preliminary observations should be made concerning the above table. First, Lease Collateral is the only creditor asserting a claim having priority under s 556(1)(c).

11 Second, insofar as Lease Collateral asserts claims having priority under s 556(1)(e), the estimated funds available for priority creditors and claimants under s 556(1)(e) is sufficient to pay all those claims in full, assuming the insolvency set-off contended for by the liquidators.

12 Third, as will be seen, the rule in *Cherry v Boultbee* requires a different approach to the netting-off of reciprocal obligations, but in the present case, the amount available for distribution exceeds the value of claims of creditors having priority under s 556(1)(c) and (e), and the practical outcome under the rule in *Cherry v Boultbee*, if applicable, is the same as insolvency set off, if applicable.

Notice of the application

13 Notice of the application has been given to relevant interested persons: (a) Lease Collateral as trustee for the Specialised Finance Warehouse Trust 1; (b) the Commonwealth Attorney-General's Department (administering the FEG), (c) Mr Hill and Mr Lord of PPB Advisory, the former receivers and managers of Force Corp, (d) each known creditor of Force Corp, of which there are three secured creditors, 356 unsecured priority creditors, and 789 unsecured creditors, and (d) the Australian Securities and Investments Commission (ASIC).

14 No response has been received from ASIC. Of the other persons notified, only Lease Collateral indicated that it sought to be heard in the proceedings. It filed a notice of intention to appear without becoming a party. At the hearing, Lease Collateral consented to an order that it be joined as a defendant to the proceedings. Lease Collateral does not put any position in contradiction to the course proposed to be taken by the liquidators and it supports the making of

the directions sought. The Commonwealth Attorney-General's Department has indicated that it does not wish to be heard on the application.

The Court's power to give directions

15 Although the winding-up of Force Corp is taken to have commenced on 13 July 2015 (ss 513B and 513C) being prior to the commencement of the *Insolvency Law Reform Act 2016* (Cth), which introduced the Insolvency Practice Schedule (Corporations), the transitional provisions in the *Corporations Act* which preserve the former statutory power to give directions under s 479 and s 511 of the *Corporations Act* do not apply because these proceedings were commenced after 1 September 2017: *Re Australian Institute of Professional Education Pty Ltd (in liq)* [2018] FCA 780; *Re PrimeSpace Property Investment Limited (in liq)* [2018] NSWSC 919 at [18].

16 Section 90-15(1) of the Insolvency Practice Schedule (Corporations) provides that the Court may make such orders as it thinks fit in relation to the external administration of a company. A company is taken to be under external administration, if, among others, a liquidator has been appointed in relation to the company: s 5-15(c). The powers of the Court under s 90-15 include making an order determining any question arising in the external administration of the company: s 90-15(3)(a).

17 It has been said that the Court's power to give directions under s 90-15 at least corresponds with and is arguably wider than its power to give directions to the liquidators under former ss 479 and 511 of the *Corporations Act*: *Walley, In the matter of Poles & Underground Pty Ltd (Admin Apptd)* [2017] FCA 486 at [41]; *Re Hawden Property Group Pty Ltd (in liq)* (2018) 125 ACSR 355; [2018] NSWSC 481; *Re Australian Institute of Professional Education Pty Limited (In Liquidation)* (2018) 334 FLR 401; [2018] NSWSC 1028 at [2]; *Re RCR Tomlinson Ltd (administrators appointed)* [2020] NSWSC 735. In this case, no reliance is placed on the possible wider scope of the power under s 90-15.

18 The function of a liquidator's application for directions is to give the liquidator advice as to the proper course of action for him or her to take in the liquidation: *Sanderson v Classic Car Insurances Pty Ltd* (1985) 10 ACLR 115 at 117; *Re Ansett Australia Ltd (Admins Apptd) and Korda* [2002] FCA 90; (2002) 40 ACSR 433 at [46].

19 The proper subject matter of an application for directions is to provide guidance on matters of law and the reasonableness of a contemplated exercise of discretion, but not a matter relating to the making or implementation of a business or commercial decision unless there is a particular legal issue raised or an attack on the propriety or reasonableness of the decision: *Sanderson v Classic Car Insurances Pty Ltd* at 117; *Re G B Nathan & Co Pty Ltd (in liq)* (1991) 24 NSWLR 674 at 686-687; *Re Ansett Australia Ltd* at 65; *Re M F Global Australia Ltd (in liq)* [2012] NSWSC 994; (2012) 267 FLR 27 at [7]. Assuming the liquidator has made full and fair disclosure to the Court of the material facts, he or she will be protected from liability for any alleged breach of duty as liquidator to a creditor or contributory or to the company in respect of anything done by him or her in accordance with the direction: *Re G B Nathan & Co* at 679.

20 I am satisfied that this is an appropriate case for directions to be given to the liquidators. The issues in respect of which directions are sought do not involve business decisions or matters of commercial judgment. Rather, the directions sought would provide guidance on complex matters of law arising in the winding-up and will protect the liquidators against accusations that they have acted contrary to law with respect to the distribution of funds to priority creditors of Force Corp. Although the relevant creditors with an interest in the distribution in the winding-up have not expressed any opposition to the proposed course to be taken by the liquidators, the liquidators have expressed the concern that they cannot be certain that there is no other information "out there" which could affect the correctness of the agreed factual position as between the liquidators and Lease Collateral: *Re Courtenay House Capital Trading Group Pty Ltd (in liquidation)* [2002] NSWSC 780 at

[7]. That concern is well-founded, given the receivers were in control of the assets of Force Corp at the time when the payments in issue occurred.

Factual background

21 Force Corp was incorporated on 21 June 2004. Force Corp operated a business that specialised in the hire of working-at-height equipment, such as elevated work platforms, vertical lifts, and travel towers within the construction industry. By mid-2015, it had 308 employees and operated at multiple locations across Australia.

22 In October 2014, Force Corp refinanced its existing secured liabilities by entering into a number of facilities totalling $72 million with Lease Collateral as trustee for the Specialised Finance Warehouse Trust 1 and a $15 million receivable financing facility Recfin in its capacity as trustee of the Recfin Series 2014-2 Trust (together the Facilities). Lease Collateral is a subsidiary of Challenger Limited. Recfin is a subsidiary of IOOF Limited.

23 As security for the Facilities advanced by Lease Collateral, Force Corp granted Lease Collateral our a first ranking security interest over all its present and after acquired property (other than its receivables, in respect of which Recfin was the only first ranking security holder for the receivables leasing facility of $15 million) with both securities registered on the Personal Property Securities Register (the Securities).

24 On 27 October 2014, a total of $77.76 million was advanced to Force Corp pursuant to the Facilities. The overwhelming majority of these funds were used to repay amounts due to the previous secured creditors.

25 Following default under the facilities in December 2014 and a standstill agreement with the secured lenders, the receivers and the administrators were each appointed as indicated on 13 July 2015.

26 During the course of the receivership, Recfin’s secured debt was repaid from recoveries from Force Corp’s accounts receivable. However, the receivers

remained in office to realise the other property, assets and undertaking of Force Corp to repay the secured debt owing to Lease Collateral. A deed of appointment of the existing receivers by Lease Collateral was prepared but never executed.

27 The issues the subject of the application for directions have been canvassed in extensive correspondence between the liquidators, Lease Collateral, and FEG over the course of almost one year. Ultimately, an agreed position was reached by those parties and the committee of inspection in the winding up of Force Corp unanimously endorsed the agreed position. As indicated, all priority creditors have been served with the application. None has taken any step to appear in the proceedings to express any opposition to the proposed course that the liquidators wish to adopt. In accordance with orders made by the Court on 24 August 2020, the liquidators have prepared a statement of agreed facts for the purposes of the proceedings (Ex F), which have been agreed with Lease Collateral.

The priority payments provision – s 556

28 *Corporations Act*, s 556 deals with the claims of priority creditors in the winding up, relevantly, in these terms:

> **556 Priority payments**
>
> (1) Subject to this Division, in the winding up of a company the following debts and claims must be paid in priority to all other unsecured debts and claims:
>
> (a) first, expenses (except deferred expenses) properly incurred by a relevant authority in preserving, realising or getting in property of the company, or in carrying on the company's business;
>
> (b) if the Court ordered the winding up—next, the costs in respect of the application for the order (including the applicant's taxed costs payable under section 466);
>
> …
>
> (c) next, the debts for which paragraph 443D(a) or (aa) entitles an administrator of the company to be indemnified (even if the administration ended before the relevant date), except

expenses covered by paragraph (a) of this subsection and deferred expenses;

(da) if the Court ordered the winding up—next, costs and expenses that are payable under subsection 475(8) out of the company's property;

…

(dd) next, any other expenses (except deferred expenses) properly incurred by a relevant authority;

(de) next, the deferred expenses;

(df) if a committee of inspection has been appointed for the purposes of the winding up—next, expenses incurred by a person as a member of the committee;

(e) subject to subsection (1A)—next:

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

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

(f) next, amounts due in respect of injury compensation, being compensation the liability for which arose before the relevant date;

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

(i) on or before the relevant date; and

(ii) because of an industrial instrument; and

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

(iv) in respect of leave of absence;

(h) subject to subsection (1C)—next, retrenchment payments payable to employees of the company.

…

Superannuation guarantee charge

(1A) The amount or total paid under paragraph (1)(e) to, or in respect of, an excluded employee of the company must be such that so much (if any) of it as is attributable to non-priority days does not exceed $2,000.

…

Leave amounts

(1B) The amount or total paid under paragraph (1)(g) to, or in respect of, an excluded employee of the company must be such that so much (if any) of it as is attributable to non-priority days does not exceed $1,500.

Retrenchment payments

(1C) A payment under paragraph (1)(h) to an excluded employee of the company must not include an amount attributable to non-priority days.

Definitions

(2) In this section:

company means a company that is being wound up.

deferred expenses, in relation to a company, means expenses properly incurred by a relevant authority, in so far as they consist of:

(a) remuneration, or fees for services, payable to the relevant authority; or

(b) expenses incurred by the relevant authority in respect of the supply of services to the relevant authority by:

(i) a partnership of which the relevant authority is a member; or

(ii) an employee of the relevant authority; or

(iii) a member or employee of such a partnership; or

(c) expenses incurred by the relevant authority in respect of the supply to the relevant authority of services that it is reasonable to expect could have instead been supplied by:

(i) the relevant authority; or

(ii) a partnership of which the relevant authority is a member; or

(iii) an employee of the relevant authority; or

(iv) a member or employee of such a partnership.

employee, in relation to a company, means a person:

(a) who has been or is an employee of the company, whether remunerated by salary, wages, commission or otherwise; and

(b) whose employment by the company commenced before the relevant date.

excluded employee, in relation to a company, means:

(a) an employee of the company who has been:

(i) at any time during the period of 12 months ending on the relevant date; or

(ii) at any time since the relevant date;

or who is, a director of the company;

(b) an employee of the company who has been:

(i) at any time during the period of 12 months ending on the relevant date; or

(ii) at any time since the relevant date;

or who is, the spouse of an employee of the kind referred to in paragraph (a); or

(c) an employee of the company who is a relative (other than a spouse) of an employee of the kind referred to in paragraph (a).

non-priority day, in relation to an excluded employee of a company, means a day on which the employee was:

(a) if paragraph (a) of the definition of excluded employee applies—a director of the company; or

(b) if paragraph (b) of that definition applies—a spouse of an employee of the kind referred to in paragraph (a) of that definition; or

(c) if paragraph (c) of that definition applies—a relative (other than a spouse) of an employee of the kind referred to in paragraph (a) of that definition;

even if the day was more than 12 months before the relevant date.

quarter has the same meaning as in the Superannuation Guarantee (Administration) Act 1992.

relevant authority, in relation to a company, means any of the following:

(a) in any case—a liquidator or provisional liquidator of the company;

(c) in any case—an administrator of the company, even if the administration ended before the winding up began;

(d) in any case—an administrator of a deed of company arrangement executed by the company, even if the deed terminated before the winding up began.

retrenchment payment, in relation to an employee of a company, means an amount payable by the company to the employee, by virtue of an industrial instrument, in respect of the termination of the employee's employment by the company, whether the amount becomes payable before, on or after the relevant date.

superannuation contribution, in relation to a company, means a contribution by the company to a fund or scheme for the purposes of making provision for, or obtaining, superannuation benefits (including defined benefits) for an employee of the company, or for dependants of such an employee.

Issue A: The funding on appointment issue

29 The agreed facts record in pars 13-15 that upon their appointment on 13 July 2015 the administrators were unfunded as the receivers took control of the assets and property of Force Corp, including circulating assets such as cash at bank. On 13 July 2015, Lease Collateral agreed to advance funds to the administrators and otherwise indemnify the administrators with respect to the conduct of the voluntary administrations of Force Corp and its subsidiaries (with professional fees limited to $250,000 (excluding GST and disbursements) and the administrators' professional fees, expenses and disbursements in connection with the proposed application to the Court for an extension of the convening period for the second meeting of creditors of Force Corp and its subsidiaries pursuant to s 439A of the Act (the Lease Collateral indemnity). The terms of the indemnity included that in the event that Force Corp was wound up and the liquidators received any recoveries from any insolvent trading claim or unfair preference claims, Lease Collateral would be reimbursed for the monies it advanced to the administrators in accordance with the indemnity.

30 The terms of the indemnity were not reduced to writing at the time, but were recorded in a letter from the liquidators as the then administrators to Lease Collateral's solicitors, Corrs Chambers Westgarth, dated 24 November 2015. Although the letter refers to previous discussions with Challenger Financial Services Group (Challenger), the reference to "Challenger" may be taken to be a reference to Lease Collateral being the entity within the Challenger Group to which the administrators issued their invoices for payment and which Lease Collateral in fact paid.

31 The total amount advanced by Lease Collateral to the administrators under the indemnity was $338,416.85, including GST (or $307,615.68 excluding GST in respect of the administrators' professional fees and disbursements comprising professional fees of $265,231, excluding GST, and reimbursement of expenses of $42,420.68, excluding GST).

32 The agreed facts record in pars [18] and [19] that the administrators received an input tax credit of $23,073.88 on the amount paid by Lease Collateral to the administrators.

33 The liquidators accept that the terms of the funding arrangement did not oblige the administrators unconditionally to repay the amounts lent by Lease Collateral; rather the arrangement was that Lease Collateral would be reimbursed from recoveries made in unfair preference or insolvent trading proceedings, in the event that Force Corp was wound up. As events have transpired, the qualification on repayment by the administrators has been satisfied since substantial recoveries have been made by the liquidators from pursuit of these claims. The affidavit of Mr Lombe indicates that total proceeds received relating to the recovery of alleged unfair preference payments total $1,973,500.

34 The liquidators submitted that the advance of funds by Lease Collateral to the administrators involved the incurring of a liability by the administrators, as they were obliged to repay the money advanced out of certain recoveries. The submission continued that the advance gave rise to a liability of the

administrators, either for monies borrowed, for the purposes of s 443A(1)(d) so as to fall within the scope of s 443D(a), or otherwise a liability incurred in good faith and without negligence by the administrators, so as to fall within s 443D(aa).

The administrator's liability for money borrowed

35 Section 443A(1) relevantly provides that the administrator of a company under administration is liable for debts he or she incurs, in the performance or exercise or purported performance or exercise, of any of his or her functions and powers as administrator, for:

> …
>
> (d) the repayment of money borrowed; or
>
> (e) interest in respect of money borrowed; or
>
> (f) borrowing costs.

36 The extension of an administrator's personal liability to repayment of money borrowed, interest in respect of that money and borrowing costs, was effected by the Corporations (Amendment) Insolvency Act 2007. The explanatory memorandum to the Corporations (Amendment) Insolvency Bill 2007 noted at par [7.194] that this provision was intended to cover not only the amount borrowed, but also interest and other expenses relating to borrowing and that through the operation of ss 443D (the administrator's right to indemnity) and 556, those debts will receive priority in a subsequent liquidation.

37 The effect of s 443D(a) is that the administrator of a company is entitled to be indemnified out the company's property (other than excluded property, being a reference to any PPSA retention of title property) for, relevantly, debts for which the administrator is liable, being the debts referred to in s 443A(1).

38 Plainly, the arrangement between Lease Collateral and the administrators entered into on 13 July 2015 involved the borrowing of monies for which the administrators were personally liable under s 443A(1)(d), albeit their liability

was limited in amount to particular recoveries by the ultimate liquidators in the event that Force Corp was wound up. In the circumstances, no occasion arises to consider whether the administrators incurred a liability that falls within s 443D(aa).

39 Where the company proceeds to liquidation, the debts for which s 443D(a) entitles the administrator is to be indemnified, receive priority under s 556(1)(c). Thus, in the present case, the administrators' liability to Lease Collateral under s 443A(1)(d) in connection with the funding advanced to them is a debt for which the administrators are entitled to be indemnified under s 443D(a), and is a priority claim within s 556(1)(c). It is an agreed fact between the liquidators and Lease Collateral that this amount is $315,342.97, being the amount advanced by Lease Collateral ($338,416.85) less the input tax credit it received ($23,073.88).

40 It is appropriate that the Court give the liquidators a direction that they would be justified in treating the administrators' debt to Lease Collateral in the amount of $315,342.97 as a priority claim by Lease Collateral within sub-sec 556(1)(c) of the *Corporations Act*.

Further facts relevant to Issues B and C

41 An understanding of Issue B, the subrogation issue, and Issue C, the offsetting claim issue, is assisted by a reference to the detailed chronology recorded in pars [20]-[33] of the agreed facts, which it is convenient to reproduce in full:

> **C. Wages paid by the Receivers from Circulating Assets**
>
> [20] As at the date of the Receivers' appointment on 13 July 2015, a total of approximately $1,515,196.12 was owing to employees of Force Corp in accordance with s 556(1)(e) of the Act for outstanding pre-appointment wages and superannuation entitlements (Total Pre-Appointment Wages and Superannuation) comprising:
>
> a. The amount of $856,515.97 that was paid by the Receivers to Force Corp's employees, or withheld as PAYG tax and remitted to the ATO or withheld as superannuation and subsequently remitted to various employee superannuation

funds, in relation to payments arising out of wage events that occurred on 14 and 15 July 2015. These entitlements were subsequently paid by the Receivers in accordance with section 433(3)(c) and section 556(1)(e) of the Act which is further discussed in paragraphs 26 to 33;

b. Unpaid pre-appointment wages in the amount of $48,622.72; and

c. Unpaid pre-appointment superannuation outstanding (excluding superannuation guarantee charge liability and superannuation on payment in lieu of notice) in the amount of $610,057.43.

[21] On 14 July 2015, Lease Collateral advanced $1 million to the Receivers to fund the receivership of Force Corp (Receiver Loan).

[22] Also on 14 July 2015 the Receivers obtained the amount of $720,280.20 by drawing down available cash from Force Corp's Receivables Purchasing Facility (Receivables Drawdown).

[23] The Receivables Drawdown was a circulating asset available to the Receivers.

[24] On or about 20 July 2015, the Receivers recovered a further amount of $682,799.58 from Force Corp's general bank accounts, petty cash and other circulating assets (Other Circulating Asset Recoveries).

[25] The circulating assets recovered by the Receivers therefore totalled $1,403,079.78, comprising the Receivables Drawdown in the amount of $720,280.20 and the Other Circulating Asset Recoveries in the amount of $682,799.58 (Total Circulating Asset Recoveries).

[26] On 14 and 15 July 2015 and 28 October 2015, the total amount of $856,515.97 was paid by the Receivers to Force Corp's employees, or withheld as PAYG tax and remitted to the ATO or withheld as superannuation and subsequently remitted to various employee superannuation funds, in relation to those payments arising out of wage events that occurred on 14 and 15 July 2015 as follows:

a. on 14 and 15 July 2015, the Receivers paid the sum of $569,284.76 to employees for preappointment wages and otherwise deferred the payment of the PAYG tax and superannuation benefits referable to those wages until October 2015;

b. on 28 October 2015, the Receivers paid the deferred PAYG tax of $207,954.24 to the ATO and paid superannuation benefits of $74,309.76 (together totalling $282,264.00) referable to the wages referred to in subparagraph 26.a above;

c. the Receivers also made deductions from the wage event that occurred on 14 and 15 July 2015 in the amount of $4,967.25 in

relation to: (i) child support amounts of $2,332.21 (which were paid on 31 July 2015); (ii) a loan repayment by an employee for the amount of $2,591.56; and (iii) other deductions for $43.48;

d. the payments in subparagraphs (a) – (c) above should total $856,515.97 and represent the amount paid to employees for pre-appointment wages and superannuation out of the Receivers' Trading Account. However, the amounts referred to subparagraphs (a) –(c) above total $856,516.01 – the 4c rounding error is attributable to differing figures from various source documents.

[27] The payments by the Receivers of the amount totalling $856,515.97 to employees of Force Corp with respect to pre-appointment wages, PAYG tax deferred on those wages, and superannuation benefits (Total Wages Payments) were paid out of the bank account maintained by the Receivers (Receivers' Trading Account), as to which:

a. on 14 and 15 July 2015, the monies in the Receivers' Trading Account were constituted by, inter alia, the Receiver Loan and the Receivables Drawdown; and

b. on 28 October 2015, the balance of the Receivers' Trading Account reflected ongoing trading by the Receivers and various receipts and payments, including the Other Circulating Asset Recoveries; however, the balance of the Receivers' Trading Account never fell below the amount of the payments totalling $282,264 that are referred to in subparagraph 26.b above.

[28] Accordingly, the Total Wages Payments in the amount of $856,515.97 were paid out of circulating assets in accordance with section 433(3)(c) of the Act.

[29] In the absence of the Receivers paying the Total Wages Payments, the sum of $856,515.97 would otherwise have been payable to Lease Collateral pursuant to its Securities (including over circulating assets). Lease Collateral is entitled to be subrogated to the position of the employees of Force Corp who were paid the Total Wages Payments.

[30] After the payment of the Total Wages Payments (which were referable to wage events that occurred on 14 and 15 July 2015), the amounts still owing to Force Corp's employees on account of pre-appointment wages and superannuation benefits was $658,680.15 (calculated as the Total Pre-Appointment Wages and Superannuation in the amount of $1,515,196.12 less the Total Wages Payments in the amount of $856,515.97).

[31] Of the Total Circulating Asset Recoveries, the Receivers failed to pay the amount of $546,563.81 (calculated as the Total Circulating Asset Recoveries in the amount of $1,403,079.78 less the Total Wages Payments in the amount of $856,515.97) to employees of Force Corp on account of wages, superannuation benefits and other employee

entitlements in accordance with section 433(3)(c) and section 556(1)(e) of the Act. The sum of $546,563.81 was instead utilised by the Receivers for other purposes and, in turn, Lease Collateral as the only secured creditor of Force Corp by this point in time (in circumstances where Recfin's secured debt had been repaid).

[32] For the purpose of this proceeding, Lease Collateral accepts that the whole of the amount of $546,563.81 ought to have been paid to meet the pre-appointment wages, superannuation benefits and other employee entitlements that remained owing to Force Corp's employees in circumstances where the amount owing to employees, after 15 July 2015, was $658,680.15 (as set out in paragraph 30 above) and therefore exceeded the sum of $546,563.81 (as set out in paragraph 31 above).

[33] For the purpose of this proceeding, Lease Collateral accepts that the amount of $546,563.81 should be set-off against the amount of $856,515.97 for which Lease Collateral is entitled to be subrogated to the position of Force Corp's employees as set out in paragraph 29 above. Accordingly, the amount payable to Lease Collateral pursuant to section 556(1)(e) of the Act in relation to the Total Wages Payments is the sum of $309,952.16 (being $856,515.97 less $546,563.81).

Issue B: The subrogation issue

42 The subrogation issue arises this way. As the agreed facts record at par [20], of the total of approximately $1,515.196.12 owing to employees of Force Corp as at 13 July 2015 for pre-appointment wages and superannuation entitlements, the receivers paid $856,515.97 out of the bank account maintained by the receivers (the receiver's trading account). Notwithstanding the different sources of monies in the receiver's trading account, the liquidators consider that the pre-appointment wages and superannuation totalling $856,515.97 were paid out of "circulating assets" in accordance with the receivers' obligation under s 443(3)(c) of the *Corporations Act*. The liquidators submit that by operation of the equitable principle of subrogation, Lease Collateral should be subrogated to the position of those employees with respect to a priority distribution in that amount pursuant to s 556(1)(e).

43 *Corporations Act*, ss 433(2) and (3), relevantly provide:

433 Property subject to circulating security interest—payment of certain debts to have priority

(2) This section applies where:

(a) a receiver is appointed on behalf of the holders of any debentures of a company or registered body that are **secured by a circulating security interest**, or possession is taken or control is assumed, by or on behalf of the holders of any debentures of a company or registered body, of any **property comprised in or subject to a circulating security interest**; and

(b) at the date of the appointment or of the taking of possession or assumption of control (in this section called the relevant date):

(i) the company or registered body has not commenced to be wound up voluntarily; and

(ii) the company or registered body has not been ordered to be wound up by the Court.

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

…

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

…

44 The provision has a long history, dating back to the *Preferred Payments in Bankruptcy Amendment Act 1897* (UK) which was designed to meet what was described by Lord Macnaghten in *Salomon v A Salomon & Co Ltd* [1897] AC 22 at 53 as "a great scandal". The root of the scandal was the widespread use of floating charges over trading stock, book debts and other circulating capital which produced a situation in which a company's business might appear to be thriving and employees and ordinary trade creditors dealt with it on that basis unaware of the existence of a floating charge. On the occurrence of a sudden and unexpected crystallisation of a floating charge, those creditors were caught unawares and deferred in the liquidation to debenture-holders who would "generally step in and sweep off everything". Parliament's response was the precursor to s 433(3)(a): as designed its scope was always limited so as to apply to floating but not fixed or "specific" charges.

45 As the High Court recognised in *Stein v Saywell* (1969) 121 CLR 529 at 544 (Barwick CJ) and 550 (McTiernan and Menzies JJ) in relation to the predecessor provisions in the *Companies Act 1961* (NSW), s 292(1)(d) and 292(4), the purpose of s 433(3)(c) of the *Corporations Act* is that employees of companies that become insolvent enjoy special priority for their unpaid entitlements, primarily in recognition that their contribution to a company may enhance the value of assets the subject of a creditor's security. That remains the position with the current provisions of the *Corporations Act*: see *Korda v Silk Chime Pty Ltd* [2010] WASC 155; (2010) 243 FLR 269 at [46]; *Saker, in the Matter of Great Southern Ltd* [2014] FCA 771 at [26]-[29]; *Jones (Liquidator) v Matrix Partners Pty Ltd, in the matter of Killarnee Civil & Concrete Contractors Pty Ltd (in liq)* (2018) 260 FCR 310; [2018] FCAFC 40 at [112]-[120]; *Kirman v RWE Robinson and Sons Pty Ltd (in liq), in the matter of RWE Robinson and Sons Pty Ltd (in liq)* [2019] FCA 372 at [40].

46 The provision has been described as a remedial provision that favours the specified priority creditors by giving them a statutory entitlement to be paid from assets that would otherwise not have been available because those assets would have become the subject of a fixed charge when the floating charge crystallises on the appointment of receivers: *CMI Industrial Pty Ltd (in liq), Re: Byrnes v CMI Ltd* [2016] 1Qd R 241; [2015] QSC 96 at [45].

47 Thus, a receiver or other controller who, or which is enforcing a circulating security interest, is required by s 433(3)(c) to pay the specified unsecured debts or amounts out of the company's property in priority to debts secured by that circulating security interest: *Great Southern Ltd (Recs and Mgrs Appted) (in liq), Re ex parte Thackaray* [2012] WASC 59; (2012) 260 FLR 362 at [10]-[11], [13].

The application of s 433

48 Section 433(2) provides a threshold requirement for the application of s 433(3)(a) of the *Corporations Act*, namely that there must be an interest secured by or subject to a "circulating security interest".

49 That phrase is defined by s 51C of the *Corporations Act* as a security interest that is either a:

(1) PPSA security interest that (i) "has attached to a circulating asset within the meaning of the *Personal Property Securities Act 2009*" and (ii) is one to which the grantor (within the meaning of that Act) has title, or

(2) floating charge (itself defined by s 9 to include a charge that conferred a floating charge at the time of its creation but subsequently became a fixed or specific charge).

50 A PPSA security interest is defined in s 51 of the *Corporations Act* in these terms:

> **51 Meaning of *PPSA security interest***
>
> In this Act:
>
> ***PPSA security interest*** (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.

51 The liquidators consider that it is appropriate to treat the payments made by the receivers referred to in the agreed facts at par [26], totalling $856,515.97 as having been made from the receivables drawn down on 14 July 2015 of $720,280.20 and the other circulating assets recoveries of $682,799.58 (see pars [22] and [24] of the agreed facts), even though the later recoveries by the receivers of $682,799.58 were intermingled with other funds in the receivers' trading account from the ongoing trading of the business by the receivers. At all times between 20 July 2015 and 28 October 2015 when the payments referred to in par [26(b) and (c)] of the agreed facts were made, the credit balance of the receivers' trading account never fell below the total amount of the relevant payments which were made on account of employees' wages and superannuation.

52 In support of this approach, the liquidators referred to the remarks of Bryson J in *Whitton v ACN 003 266 886 Pty Ltd (Controller appointed) (in liq)* (1996) 42 NSWLR 123, that a receiver is not obliged to effectively segregate or trace the proceeds of circulating assets and to pay employees from assets of that type, as opposed to making the payment from other funds that can later be augmented by the recovery of circulating assets. I accept that submission. As Bryson J said at 137:

> For most assets subject to floating charges some process of conversion into money must be carried out by the controller before a payment can be made. Even a book debt must be collected, and for many classes of property it is necessary to carry out processes which may involve expenditure in order to convert them into money. I would think that there would be no breach of the subsection [433(3)(c)] if a controller effected conversion into money by valuing the property subject to a floating charge and appropriating the same amount of money in his hands from some other source to payment of the priority debts. With respect I do not think that it can be correct to suppose that it is the controller's duty immediately to convert the very assets subject to a floating charge into money by selling those assets for the purpose of paying the priority debts; that might tear the heart out of the company's business and affairs and defeat the prospects of successful administration in the interest of anybody else, and I do not find it possible to suppose that that was the legislature's purpose in enacting subs 433(3); it must have been contemplated that some process of conversion would take place as part of the whole process of winding-up even if that involved some delay, or some expense.

53 Turning to the question of the nature of the assets recovered by the receivers and whether or not they were circulating assets of the company, s 340 of the *Personal Property Securities Act 2009* (Cth) (the PPSA) is, relevantly, in these terms:

> **340 Meaning of circulating asset**
>
> *General definition*
>
> (1) For the purposes of this Act, if a grantor grants a security interest in personal property to a secured party, the personal property is a ***circulating asset*** if:
>
> (a) the personal property is covered by subsection (5) (unless subsection (2) or (3) applies); or
>
> (b) in any other case – the secured party has given the grantor express or implied authority for any transfer of the personal

property to be made, in the ordinary course of the grantor's business, free of the security interest.

…

Current assets

(5) This subsection covers the following personal property:

(a) an account that arises from granting a right, or providing services, in the ordinary course of a business of granting rights or providing services of that kind (whether or not the account debtor is the person to whom the right is granted or the services are provided);

(b) an account that is the proceeds of inventory;

(c) an ADI account (other than a term deposit);

(d) currency;

(e) inventory;

(f) a negotiable instrument.

54 The recoveries of money in bank accounts, which for the most part constituted the other circulating asset recoveries of $628,799.58 answer the description of "circulating assets": s 304(5)(c) of the PPSA.

55 The proceeds of the receivables drawdown of $720,280.20 were actually recovered and received by the receivers, in contrast to the position in *Re RCR Tomlinson Ltd (administrators appointed)* [2020] NSWSC 735 where Black J held that unexercised rights to require payments of money were not equivalent to rights to *receive* payments of money and were relevantly not circulating assets at [105]-[106].

56 The proceeds of the receivables drawdown answer the description of "circulating assets", being an asset that fell within s 340(5)(b) of the PPSA, as an account that was the proceeds of inventory, given the definition of "proceeds" in s 31(1)(a) of the PPSA, which relevantly provides:

"proceeds" of collateral to which a security interest is (or is to be) attached means identifiable or traceable personal property of the following types, …:

> (a) personal property that is derived directly or indirectly from a dealing with the collateral (or proceeds of the collateral);
>
> …

and "collateral" is defined in s 10 of the PPSA to mean "personal property to which a security interest is attached", and "personal property" is widely defined to mean property (including a licence) other than (a) land or (b) a right, entitlement or authority granted by or under a law of the Commonwealth, a State or a Territory, and declared by that law not to be personal property for the purposes of the PPSA.

57 The next question is whether either of the exceptions to the definition of circulating asset contained in s 340(2) and (3) of the PPSA applies, namely:

> …
>
> Exceptions
>
> (2) Despite paragraph (1)(a), personal property covered by subsection (5) is not a circulating asset if:
>
> (a) an effective registration with respect to the property, in relation to the grantor, discloses, in accordance with the regulations, that the secured party has control of the personal property; and
>
> (b) the secured party has control of the personal property.
>
> Note: For the meaning of control in this subsection, see section 341.
>
> (3) Despite subsection (1), personal property covered by subsection (5) is not a circulating asset if:
>
> (a) the personal property is goods; and
>
> (b) the security interest is perfected by possession.

58 As to the issue of control in s 340(2), I accept the liquidators' submission that the general terms of the receivables purchasing agreement and the financing statements lodged on the Personal Property and Securities Register by Lease Collateral and Recfin demonstrate that no control was exercised over the account of Force Corp into which the receivables drawdown was paid.

59 The exception in relation to “goods” in s 340(3) of the PPSA has no application because the circulating assets in the present case were not “goods”.

60 The proceeds of the receivables drawdown and the other circulating asset recoveries are circulating assets they fell within the terms of the general security deed dated 17 August 2014 granted by Force Corp in favour of Lease Collateral: see cl 3.1(b). This security interest was a PPSA security interest for the purposes of s 51 of the *Corporations Act*.

61 Accepting that the receivers recovered circulating assets, the effect of s 433(3)(c) is to require a receiver to prioritise the payment of claims of employees, including those that would fall under s 556(1)(e), ahead of those of a secured creditor with respect to property that is comprised in or subject to a circulating security interest.

62 It may be inferred, that in recognition of the obligation contained in s 433(3)(c), the receivers used the proceeds of the receivables drawdown to make the payments to employees on 14 and 15 July 2015, rather than pay these amounts to Lease Collateral. The position is the same with respect to the payments made to or for the benefit of employees from the receivers' trading account later in July 2015 and on 28 October 2015: see the agreed facts at [26(b) and (c)]. The effect was two-fold. First, there was a lesser amount of money available for distribution to Lease Collateral. Second, the value of the Lease Collateral security interest was diminished.

63 Had the receivers not made the payments to employees on account of pre-appointment wages and superannuation, Lease Collateral would have received those sums and Force Corp's outstanding indebtedness to Lease Collateral in the winding up would have been reduced.

64 The liquidator says that in these circumstances the equitable principles of subrogation are applicable. That is, a secured creditor, the value of whose security is diminished by the payment to employees out of circulating assets

that form part of the secured property, is entitled to be subrogated to the position of the employees who were paid from the circulating assets in accordance with s 433(3)(c) of the *Corporations Act*: *Divitkos, in the matter of XDVD Pty Ltd (in liq)* [2014] FCA 696; (2014) 223 FCR 409 at [63]-[68]; *Western (Liquidator); In the matter of 7 Steel Distribution Pty Limited (in liq)* [2015] FCA 742 at [28]-[29]; *Blakely, In the matter of Akron Roads Pty Ltd (in liq)* [2020] FCA 1378 at [30]-[34].

Subrogation

65 The doctrinal basis of equitable subrogation in Australian law is stated in *Bofinger v Kingsway Group Limited* (2009) 239 CLR 269; [2009] HCA 94 at [85]-[98], where the High Court rejected the “unjust” enrichment concept adopted in English authorities such as *Banque Financiere de la Cite v Parc (Battersea) Ltd* [1999] 1 AC 221.

66 In *Aged Care Services Pty Ltd v Kanning Services Pty Ltd* (2013) 86 NSWLR 174; [2013] NSWCA 393, I said at [49] (Meagher and Leeming JJA agreeing), that subrogation is the "process by which one party is substituted for another so that he may enforce the other's rights against a third party for his own benefit" (sic): C Mitchell, *The Law of Subrogation*, Clarendon Press, Oxford (1994) at 3, cited with approval by Santow J in *Highland v Exception Holdings Pty Ltd (in liq)* [2006] NSWCA 318; (2007) 60 ACSR 223 at [90].

67 In *XDVD*, White J said at [77] that the situation of a secured creditor or of a receiver appointed to a company by a secured creditor who, in accordance with s 433 of the *Corporations Act*, makes payments to priority creditors, is analogous to that of a person who, other than voluntarily, discharges the security of another, and that is a well-recognised circumstance in which rights of subrogation arise. I agree.

68 White J continued in *XDVD* at [77]-[79]:

> [77] … The payers in such circumstances are presumed to have preserved the security for their own benefit: *Ghana Commercial Bank v Chandiram* [1960] AC 732 at 745; *Cochrane v Cochrane* [1985] 3

NSWLR 403. In the latter case, Kearney J stated the principle as follows (at 405):

> This principle is based on equity's concern to prevent one party obtaining an advantage at the expense of another which in the circumstances of the case is unconscionable. Hence, there is a common thread running through the relevant cases to the effect that the conscience of the mortgagor should be affected so as to cause the mortgage to be kept alive. This is illustrated in the text book examples first, of a third party not being entitled to a right by way of subrogation where he simply lends the money on an unsecured basis to the mortgagor who then uses such funds to pay off the mortgage; and secondly, of a third party being so entitled where he advances the money to pay out the mortgage on the understanding that security would be provided for such advance upon the mortgage being paid out. (Emphasis added.)

[78] In my opinion, there is no difficulty in imputing the requisite intention to receivers in circumstances like the present. They are quite different from strangers or volunteers who discharge the security of another. Receivers exercise their duties in the interests of their appointors, as well as in the interests of the company to which they are appointed. Rather than intending the loss of a security, their function is to preserve and realise the security. It would be inappropriate to impute an intention by them to forego that security when they make payments required by law. For the unsecured creditors or for the company itself to seek to have the benefit of the compulsory payment would, in my opinion, be both opportunistic and unconscionable.

[79] Accordingly, although the present may be a new class of case, I consider that an equitable right of subrogation should be recognised. The effect is that CBA is subrogated, to the extent that the Receivers' payments to the priority creditors diminished its security, to the entitlements of those creditors to the free funds.

69 Given that the receivers paid the amount of $856,515.97 to employees for pre-appointment wages and superannuation from circulating assets that would otherwise have been covered by Lease Collateral's security interest then, subject to the proposed set-off referred to in Issue C below, the liquidators would be justified in treating Lease Collateral as entitled to be subrogated to the position of those employees with respect to a priority distribution in that amount pursuant to s 556(1)(e) of the *Corporations Act*.

C. The offsetting claim issue

70 The liquidators submitted that the amount of the priority distribution to Lease Collateral of $856,515.97 under s 561(e) should be reduced on

account of a liability of Lease Collateral to Force Corp arising in the following circumstances.

71 The agreed facts record that $1,403,079.78 was recovered by the receivers from the circulating assets of Force Corp comprising $720,280.20 (the receivables drawdown) and $682,799.58 (the other circulating asset recoveries), but only an amount of $856,515.97 was paid by the receivers to Force Corp's employees, or withheld as PAYG tax and remitted to the ATO, or withheld as superannuation and subsequently remitted to various employee superannuation funds.

72 The difference between the total of the circulating asset recoveries of $1,403,079.78, which ought to have been applied to meet pre-appointment employees' wages and entitlements, and the amount of $856,515.97 that was so applied, being $546,563.81, was used as part of the receivership and was ultimately paid to or for the benefit of Lease Collateral. As a consequence, the receivers breached their statutory duty under s 433(3)(c) of the *Corporations Act* and are liable to restore this amount to Force Corp: *Westminster Corporation v Haste* [1950] Ch 442; [1950] 2 All ER 65; *Inland Revenue Commissioners v Goldblatt* [1972] Ch 498; [1972] 2 All ER 202; *Steinberg v Herbert* (1988) 14 ACLR 80 at 96; *Whitton* at 137B.

73 The liquidators submitted that apart from the receivers' liability, there is good reason to consider that Lease Collateral would also be liable to Force Corp for the amount that the receivers failed to pay to employees, either on accessorial grounds because it was "involved" in the contravention by the receivers, or otherwise pursuant to restitutionary principles as the recipient of the monies that were applied by mistake in breach of statutory duty. The latter analysis is the more natural way of characterising what occurred here.

74 Thus, where money is paid by reason of mistake, the payer may recover it from the recipient in a common law action for money had and received: *Australian Financial Services Leasing Pty Ltd v Hills Industries Ltd* (2014) 253 CLR 260 at 568; [2014] HCA 14. Although recovery by the claimant may

depend upon whether it would be inequitable for the recipient to retain the benefit, it is not necessary for the claimant to allege or prove that the retention of the money received by the defendant would be unjust as that is a matter on which the defendant bears the onus: *Hills Industries* at 593; *David Securities Pty Ltd v Commonwealth Bank of Australia* (1992) 175 CLR 353 at 379; [1992] HCA 48 at [57].

75 Lease Collateral accepts for the purpose of this proceeding that it has a liability to Force Corp with respect to the sum of $546,563.81 and joined with the liquidators in submitting that this amount can be offset against the amount for which Lease Collateral would be otherwise entitled as a priority distribution under s 556(1)(e). Lease Collateral accepts that the effect of the setoff would be that its priority claim under s 556(1)(e) in relation to wages paid to employees is $309,952.16 (being $856,515.97 less $546,563.81).

76 The liquidators seek a direction that they are justified in proceeding on this basis. As indicated, the liquidators initially submitted that set-off under s 553C(1) is available. Prior to the hearing the Court raised with the parties the question whether the rule in *Cherry v Boultbee* [1839] Eng R 1099; (1839) 41 ER 171 applied. The liquidators provided supplementary submissions which maintained their contention that it was arguable that Lease Collateral is entitled to the right of set-off under s 553C(1), but alternatively, the rule in *Cherry v Boultbee* was applicable. Counsel for Lease Collateral adopted the liquidators' submissions.

77 In supplementary submissions served after the hearing, the liquidators advanced an alternative submission that equitable set-off may apply in the present case if insolvency set-off is not available. Reference was made to obiter statements in *Hamersley Iron Pty Ltd v Forge Group Power Pty Ltd (in Liquidation) (receivers and managers appointed)* (2018) 53 WAR 325; [2018] WASCA 163 at [155]-[177], that insolvency set-off under s 553C is not a code and does not exclude, at least in some cases, equitable set-off where s 553C(1) is not applicable, such as because of an absence of mutuality.

(1) Insolvency set-off

78 *Corporations Act*, s 553C provides:

> **553C 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.

79 The object of insolvency set-off is to do substantial justice between the parties: *Gye v McIntyre* (1991) 171 CLR 609 at 618-619; [1991] HCA 60. Thus it has been said that insolvency set-off should be given its widest possible scope: *Gye v McIntyre* at 619; *Coventry v Charter Pacific Corp Ltd* (2005) 227 CLR 234; [2005] HCA 67 at [56]. Nonetheless, set-off is to be confined within its limits. As the joint judgment in *Coventry v Charter Pacific Corp* said at [56] (in the context of bankruptcy set-off):

> One of the limits is that creditors of the bankrupt should not be disadvantaged by allowing set-off where the debts, credits or other dealings were not genuinely mutual as a matter of substance.

80 Some of the principles concerning insolvency set-off under s 553C are referred to in *Re Hawden Property Group Pty Ltd (in liq)* [2018] NSWSC 481; (2018) 125 ACSR 355 at [27]–[31]. In the present context, four matters should be emphasised.

81 First, insolvency set-off is self-executing in the sense that it operates automatically upon the occurrence of the winding up so as to bring about an extinguishment of the claims at that date to the extent of the set-off: *Gye v McIntyre* at 622; *GM & MA Pearce & Co Pty Ltd v RGM Australia Pty Ltd* [1990] 4 VR 888 at 891, 896, 899.

82 Second, the relevant date for determining whether the sum due from one party is to be set off against any sum due from the other party in respect of mutual dealings is the "relevant date" under s 553 for determining what claims are admissible to proof against the company: *Re Parker* (1997) 80 FCR 1 at 15; *JLF Bakeries Pty Ltd v Baker's Delight Holdings Ltd* [2007] NSWSC 894; (2007) 64 ACSR 633; *Façade Treatment Engineering Pty Ltd v Multiplex Constructions Pty Ltd* [2016] VSCA 247; 116 ACSR 493. That is also the date at which the winding-up of Force Corp is taken to have commenced: s 513B(b) and 513C(b).

83 Third, the "account" in accordance with s 553C(1) must be taken whenever it is necessary for any purpose to ascertain the effect which the section had: *Gye v McIntyre* at 622; *Stein v Blake* [1995] 1 AC 243 at 253. The account shall be deemed to be taken and the sums due from one party set-off against the other as at the date of the winding up: *Stein v Blake* at 255. The respective claims cease to have a separate existence as choses in action, and are replaced by a claim to a net balance: *Stein v Blake* at 255; *Pearce & Co v RGM Australia* at 891, 896, 899. This reasoning had been applied by Beaumont J, prior to *Stein v Blake*, in *Gye v McIntyre* (FCA, Beaumont J, 8 October 1992).

84 Fourth, debts in respect of mutual dealings which may be set-off under s 553C(1) include not only debts that are then due, but debts which are contingent and which ultimately mature into pecuniary demands: *Hiley v Peoples Prudential Assurance Co Ltd* (1938) 60 CLR 468 at 497: [1938] HCA 40; *Gye v McIntyre* at 624. As to the concept of "contingent debt", it is well-established that a company will owe or be owed a contingent debt if, as a result of an existing obligation, the company will be liable to pay or be entitled

to receive a sum of money on the occurrence of a future event which may happen, not which must happen: *Community Development Pty Ltd v Engwirda Construction Co* (1996) 120 CLR 455 at 459; *Federal Commissioner of Taxation v Gosstray* [1986] VR 876 at 878.

Whether mutual dealings?

85 The liquidators' argument in support of insolvency set-off under s 553C(1) rested on an analogy with cases involving mutual dealings where debts were contingent at the date of the commencement of the winding-up, but ultimately matured into pecuniary demands: see, for example, *Shirlaw v Lewis* (1993) 10 ACSR 288 and *JLF Bakeries Pty Ltd v Baker's Delight Holdings Ltd.* That is not the present case.

86 *Shirlaw v Lewis* involved a contract for the sale of a business which provided that if the purchaser defaulted, the vendor would repurchase the purchaser's goods and saleable stock. The purchaser repudiated the contract and this was followed by a winding-up application and a liquidator was appointed. The vendor took possession of the stock and disposed of it after the filing of the winding-up application. The liquidator of the purchaser made a claim that the sale of the stock to the vendor after the commencement of the winding-up was a void disposition under a predecessor provision to s 468(1) of the *Corporations Act* and sought damages in conversion. Hodgson J found that the vendor could set-off its cross-claim for damages against the purchaser arising from repudiation against the liquidator's claim against the vendor, whether the claim was characterised as a claim in conversion or a claim based on unjust enrichment. His Honour reasoned at 296 that, "[w]hat ultimately happened after the crystallisation of mutual obligations" arose out of pre-liquidation dealings of the parties and that "these mutual obligations as crystallised are matters which would be set-off" under the applicable insolvency set-off provision; at that time s 86 of the *Bankruptcy Act 1966* (Cth).

87 This reasoning has been criticised on the basis that whilst there were prior obligations by reason of the contract, that should not have sufficed for a contingent liability and therefore for a set-off: R Derham, "Set-off against statutory avoidance and insolvent trading claims in company liquidation" (2015) 89 ALJ 459 at 481.

88 *JLF Bakeries Pty Ltd v Baker's Delight Holdings Ltd* involved a set-off under s 553C of the *Corporations Act* of monies payable after the commencement of the winding-up pursuant to the exercise of an option to purchase the insolvent company's assets against debts owed by the company to the optionee. The debts were in respect of mutual dealings, one of which was contingent on the termination of an agreement and the exercise of an option ultimately matured into a pecuniary demand. Again, that is not the present case.

89 The liquidators also referred by analogy to cases which have held or suggested that a set-off under s 553C may be available in relation to statutory recovery claims by a liquidator which only arise on the winding-up of the company, such as the recovery of compensation for loss resulting from insolvent trading under s 588M and s 588W and uncommercial transactions which are voidable under s 588FF. In *Hussain v CSR Building Products Ltd* [2016] FCA 392; 246 FCR 62, an unfair preference case, Edelman J identified a number of such cases at [227], including:

- *Re Parker*, 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;

- *Smith (in his capacity as liquidator of ACN 002 864 002 Pty Ltd (in liq) (formerly known as Petrolink Pty Ltd) v Boné* [2015] FCA 319 where Gleeson J in the Federal Court allowed a set-off to a liquidator's claim for recovery of compensation for insolvent trading under ss 588G and 588M;

- *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd* (2011) 81 NSWLR 47; [2011] NSWCA 109, where Young JA said in obiter at [279], that set off would have been allowed under s 553C to a liquidator's claim under s 588FF(1) for an uncommercial transaction. Hodgson JA agreed "substantially", and Whealy JA agreed with Young JA;

- *Hall v Poolman* (2007) NSWSC 1330; (2007) 65 ACSR 123, where Palmer J allowed a set-off under s 553C to a liquidator's insolvent trading claim of a director under ss 588G and 588M: at [408]-[414].

90 These cases are controversial. Moreover, the "creeping assumption" from the insolvent trading cases under ss 588M and 588V to the avoidance cases under s 588F, such as *Buzzle Operations*, that the reasoning in *Re Parker* is applicable to liquidator's claims under s 588FF is suspect. One difficulty with the obiter statement of Young JA in *Buzzle Operations* is the reliance upon the liquidator being an officer of the court (which is no doubt correct in a court ordered winding up) for the proposition that for the court not to allow a set off in that case would be to permit the liquidator as its officer to act inequitably: at [259]. But s 553C which is self-executing, is confined within its limits: see [79] and [81] above. There is no room for the operation of a wider principle that set off will be allowed to prevent a liquidator acting inequitably.

91 In *Bryant, in the matter of Gunns Limited (in Liq) (receivers and managers appointed) v Bluewood Industries Pty Ltd* [2020] FCA 714, an unfair preference case, Davies J did not decide whether insolvency set-off was available to an unfair preference, holding that s 553C(2) excluded any set-off on the facts, but said at [130], with reference to the remarks of Edelman J in *Hussain v CSR Building Products*:

> Justice Edelman was of the view that there were "powerful contrary arguments … to suggest that a set-off is not available against a liquidator's claim to recover preference payments" (at 107 [235]), but his Honour ultimately did not decide the point because, amongst other reasons, the Court did not have the benefit of full argument on the issue.

92 More recently in *Stone v Melrose Cranes & Rigging Pty Ltd, in the matter of Cardinal Project Services Pty Ltd (in liq) (No 2)* [2018] FCA 530; (2018) 125 ACSR 406, Markovic J followed the decision in *Re Parker*, *Buzzle Operations* and *Hall v Poolman* and held that set-off under s 553C(1) can be utilised in voidable transaction claims for an unfair preference: at [283].

93 The application of insolvency set-off to a claim by a liquidator for recovery of an unfair preference under s 588FF is contrary to a long line of authority that the right of set-off under s 553C (and predecessor provisions) is not available in unfair preference claims. In *Gunns Limited (in Liq) (receivers and managers appointed) v Bluewood Industries Pty Ltd*, Davies J referred at [130] to the following cases, by way of example: *Re a Debtor* [1927] 1 Ch 410; *Re Clements; Ex parte Trustee; Goldsbrough Mort & Co Ltd (Respondent)* (1931) 7 ABC 255; *Re Smith; Ex parte Trustee; J Bird Pty Ltd and Tully (Respondents)* (1933) 6 ABC 49; *Calzaturuficio Zenith Pty Ltd (in liq) v NSW Leather & Trading Co Pty Ltd; Victorian Leather Co Pty Ltd* [1970] VR 605; *Painter v Charles Whiting & Chambers Ltd* (1932) 4 ABC 203; and *Re Buchanan Enterprises Pty Ltd (No 2)* (1982) 7 ACLR 407.

94 The essential reasons for denying insolvency set-off with respect to a preference claim are first, the debt the subject of the preference is not provable in the liquidation until the preference payment is paid back in full, second, the obligation to repay the preference arises after liquidation, and third, there is a lack of mutuality.

95 As to the first reason, it was well-accepted under the former companies legislation, that a creditor who received an unfair preference which is set aside by order of the Court, could not prove in the winding-up of the company until the creditor had repaid the preference in full: *NA Kratzmann Pty Ltd v Tucker, Liquidator of Reid Murray Developments (Qld) Pty Ltd (No 2)* (1968) 123 CLR 295 at 297; [1968] HCA 44. The practice in *Kratzmann*'s case is now reflected in s 588FI of the *Corporations Act*.

96 It does not seem that any of the cases referred to at [93] above, or *Kratzman's* case, or s 588FI were brought to the Court's attention in *Stone v Melrose Cranes & Rigging*.

97 Accepting that the language of the avoidance provision in s 588FF is different in some respects to the predecessor provisions, it is difficult to read those differences as having the effect that s 588FF was intended to do away with the principles embodied in these earlier cases. The terms of s 588FI is a strong indicator to the contrary that the legislature did not intend to change the law in this respect. And the language of s 553C itself does not support the availability of set off to an unfair preference claim for the reasons shortly stated at [94] above.

98 The powerful contrary arguments to *Re Parker* and similar authorities to which Edelman J referred in *Hussain v CSR Building Products*, include those articulated by R Derham in *The Law of Set-Off* (4th ed (2010), Oxford University Press) at [13.21]–[13.27], and in his later article referred to at [84] above. In my view, there is much force in Mr Derham's detailed analysis and criticism of the the cases that have allowed insolvency set off under s 553C with respect to liquidator's claims for compensation under ss 588M and 588V and an uncommercial transaction claim under s 588FF. However, it is not necessary to decide this question in the present case, because there is no close or useful analogy in the present case with those type of recovery claims by a liquidator.

99 Here, the liability of Lease Collateral to Force Corp does not answer the description in s 553C(1) of a "mutual debt" or other "mutual dealings" between Force Corp and Lease Collateral, being the person who seeks to have a claim admitted against Force Corp in the liquidation. The payments made to Lease Collateral by the receivers from the proceeds of Force Corp's circulating assets, which Lease Collateral accepts that it is liable to repay to Force Corp, were received by Lease Collateral *after* the appointment of the receivers in consequence of a contravention by the receivers of the statutory obligation imposed on them by s 433(3)(c) of the *Corporations Act*.

100 The giving of credit by Force Corp to Lease Collateral after the commencement of the winding up on 15 July 2015, in the form of the mistaken payment by the receivers to Lease Collateral from the proceeds of Force Corp's circulating assets, was not referable to a transaction between Lease Collateral and Force Corp prior to the commencement of the winding up. That Lease Collateral was a secured creditor is not to the point. The transaction by which Lease Collateral is liable in debt to Force Corp is the mistaken payment by the receivers in contravention of s 433(3)(c) of the *Corporations Act*. Nor does Force Corp's claim against Lease Collateral involve a debt that was contingent before the commencement of the winding-up which ultimately matured into a pecuniary demand.

Notice of insolvency

101 Let it be assumed, however, that s 553C(1) applies. The question would then arise whether insolvency set-off is excluded by s 553C(2) because, at the time of Lease Collateral receiving credit from Force Corp Lease Collateral had notice of the fact that Force Corp was insolvent.

102 In *Jetaway Logistics Pty Ltd v Deputy Commissioner of Taxation* [2009] VSCA 319; 26 VR 657, the Victorian Court of Appeal said of the concept of "notice of the fact" in s 553C(2) at [21]–[22]:

> [21] The section requires proof, not that the creditor at the relevant time knew that the company was insolvent, but that the creditor had notice of that fact. … A person will have "notice of the fact" that a company is insolvent if the person has actual notice of facts which disclose that the company lacks the ability to pay its debts when they fall due, within the meaning of s 95A. It is unnecessary to show that the person actually formed the view that the company lacked that ability. As the NSW Court of Appeal said in *Hathaway Shirt Co Pty Ltd v B Rawe GmbH Co* [[1989] NSWCA 98], it is "well established that there is a difference in law between receiving notice of a fact and being made fully and subjectively aware of the fact".
>
> [22] 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.

103 The relevant time at which the creditor or debtor is required to have had notice of facts that would have indicated to a reasonable person that the company lacked the ability to pay its debts when they fell due is at the time of giving or receiving credit. Ordinarily, this would be when the transaction that gave rise to the liability occurred: *Old Style Confections Pty Ltd v Microbyte Investments Pty Ltd (In liq)* (1995) 2 VR 457 at 464; *Grapecorp Management Pty Ltd (in liq) v Grape Exchange Management Euston Pty Ltd* (2012) 265 FLR 33; [2012] VSC 112 at [72]-[76].

104 It has been said that the fact that administrators have been appointed to a company is not of itself conclusive evidence establishing that a party has notice of the fact that a company is insolvent from that date onwards: *JLF Bakeries Pty Ltd* at [32], although in that case, White J acknowledged, that where the administrators ceased to trade the business, there was a strong point of insolvency.

105 The onus of establishing notice of insolvency for the purposes of s 553C(2) rests on the party that resists set-off: *Jetaway Logistics Pty Ltd v Deputy Commissioner of Taxation* at [21]. In supplementary submissions filed after the hearing, the liquidators sought to resist a set-off by Lease Collateral relying upon s 553C(2).

106 The liquidators accepted that nothing in the agreed statement of facts, nor the evidence in Mr Lombe's affidavit, sheds light on the extent to which Lease Collateral had notice of the facts that would have indicated that Force Corp was insolvent following the appointment of the receivers and the administrators. Nonetheless, the liquidators submitted that in circumstances where Lease Collateral was the principal secured creditor of Force Corp, and had itself appointed the administrators, it would not be appropriate for the Court to proceed on the basis that Lease Collateral did not have notice of insolvency when it received payments from the receivers, which was at a date later than the appointment of the receivers and the administrators. The liquidators submitted that s 553C(2) may apply in the present case so as to prevent the operation of an insolvency set-off.

107 Lease Collateral was given the opportunity to make further submissions on this issue. It adopted the liquidators' submissions and confirmed that it does not seek to adduce any further evidence on whether it had notice of the fact that Force Corp was insolvent at the time the relevant payments were made. In these circumstances, the liquidators' submissions on notice should be accepted. Accordingly, if, contrary to my view, s 553C(1) is applicable, set-off would be precluded by s 553C(2).

(2) Equitable set-off

108 The classic statement of the nature of equitable set-off is that it requires "some equitable ground for being protected against" another's demand and the mere existence of cross demands is not sufficient. It is an indispensable requirement of equitable set-off that the defendant's counter claim actually goes to the root of, and essentially be bound up with, so much of the plaintiff's claim as to "impeach" the title of the plaintiff's claim: *Hawes v Dean* [2014] NSWCA 380 at [61]-[62] citing Lord Cottenham LC in *Rawson v Samuel* (1841) Cr & Ph 161; 41 ER 451 at 458, referred to with approval by the High Court in *Hill v Ziymack* (1908) 7 CLR 352 at 361; [1908] HCA 13.

109 The "impeachment of title" test remains applicable in Australia: *HP Mercantile Pty Ltd v Dierickx* [2013] NSWCA 479; (2013) 306 ALR 53 at [136], *Hawes v Dean* at [61]-[62]; *Wollongong Coal Ltd v Gujarat NRE India Pty Ltd* [2019] NSWCA 135 at [113] (Leeming JA, Bathurst CJ and McCallum JA agreeing).

110 As Emmett JA said in *HP Mercantile* at [136] (Beazley P and Meagher JA agreeing on this point) said:

> For there to be an equitable set-off, the set-off must essentially be bound up with and go to the root of, challenge, call in question, or impeach the title of the claimant. Equitable set-off is available where the party seeking it can show a recognised equitable ground for being, to the relevant extent, protected from its adversary's demand. The mere existence of a cross-claim is not sufficient. There must be some ground for equitable intervention beyond the mere existence of a cross-claim, such that it can be said that the equity of the defendant impeaches the claimant's title to the legal demand being enforced.

111 In *Wollongong Coal*, the Court of Appeal expressly refrained from deciding whether, in order for a debt to impeach another it is sufficient that it be found to be "unconscionable" to permit the enforcement of one without regard to the other. As Leeming JA said at [113], the term "unconscionable" is used in quite difference senses in equity and the notion of being contrary to good conscience as a theme explaining the availability of the equitable defence of set-off is not the same as factors sufficient to entitle a party to rescind a transaction relying upon an *Amadio* special disadvantage. The present case does not give rise to this question.

112 The liquidators submitted that Lease Collateral's obligation to make restitution to Force Corp for monies received by it in the external administration (which ought to have been used by the receivers to pay employee creditors) is inextricably bound up with its right to be subrogated in equity to the position of those same employee creditors to receive a distribution in the winding-up of Force Corp. I do not agree.

113 On the agreed facts, Lease Collateral is obliged to make restitution to Force Corp for monies paid to it by the receivers by mistake totalling $546,563.81, which ought to have been used to pay the pre-appointment wages and superannuation contributions of certain employees. That Lease Collateral is entitled to be subrogated to the claims of other employee creditors in the winding-up to priority payment under s 556(1)(e) by reason of payments made by the receivers totalling $856,515.97 to those "other" employees of Force Corp, does not answer the description of a counter-claim which goes to the root of, and impeaches the title of Force Corp's restitutionary claim against Lease Collateral in relation to the $546,563.81 received by Lease Collateral.

114 In the circumstances, it is not necessary to consider whether as a matter of principle equitable set-off may be available when there is no insolvency set-off under s 553C(1) as suggested in obiter statements in *Hammersley Iron*.

(3) The rule in Cherry v Boultbee

115 As indicated, the liquidator contends, in the alternative, that if insolvency set-off is not available, then the rule in *Cherry v Boultbee* is enlivened and the result is the same, at least in substance; namely, Lease Collateral's entitlement to a distribution in the winding up as a priority creditor is subject to its obligation notionally to pay or contribute $546,563.81 to Force Corp, with those amounts to be netted-off against one another.

116 Insolvency set-off under s 553C and the equitable principle in *Cherry v Boultbee* cover different fields and although the equitable principle continues to apply in liquidations notwithstanding the terms of s 553C, the principle in *Cherry v Boultbee* only applies where insolvency set-off is not available: *Re Anglican Development Fund Diocese of Bathurst (receivers & managers appointed)* [2015] NSWSC 44; (2015) 33 ACLC 15-010 at [37]-[39]; *Hawden Property* at [41]-[42]; *Re PrimeSpace Property Investment Limited (in liquidation)* [2018] NSWSC 919 at [27] (Black J).

117 The nature and operation of the rule in *Cherry v Boultbee* is addressed in *Re Hawden Property Group Pty Ltd (in liq)* [2108] NSWSC 481; (2018) 125 ACSR 355. Relevantly for the present context, it is convenient to reproduce what I said at [37]–[43]:

> [37] The so-called "rule in *Cherry v Boultbee*" is a somewhat inaccurate expression. The rule originated in *Jeffs v Wood* (1722) 24 ER 668 and *Cherry v Boultbee* is in fact an example of an exception to the rule. So much is clear from the analysis of the authorities by Palmer J in *Otis Elevator Co Pty Ltd v Guide Rails Pty Ltd (in liquidation)* (2004) 49 ACSR 531; [2004] NSWSC 383 at [33]-[47]. See also *In Re Kaupthing Singer & Friedlander Ltd (In Administration)* [2011] UKSC 48; [2012] 1 AC 804 at [13]-[20]. While the rule originally developed in the context of deceased estates, it has been subsequently applied in bankruptcy and company liquidations.
>
> [38] In *Re Peruvian Railway Construction Company Ltd* [1915] 2 Ch 144, Sargant J, at 150, described the rule in the following terms:
>
>> … where a person entitled to participate in a fund is also bound to make a contribution in aid of that fund, he cannot be allowed so to participate unless and until he has fulfilled his duty to contribute.

> [39] This description of the rule was adopted in *Gray v Gray* [2004] NSWCA 408 by Young CJ in Eq (Sheller and Bryson JJA agreeing) at [90]. Young CJ in Eq also observed at [91] that the rule was an illustration of a more fundamental principle of equity, that he who seeks equity must do equity.
>
> [40] More recently, Lord Walker observed *In Re Kaupthing Singer & Friedlander* that the rule is not a complex technical rule and does nothing more than provide a method of netting-off reciprocal monetary obligations. Lord Walker said at [8]:
>
> > The expression "the rule in *Cherry v Boultbee*" suggests a technical rule of some complexity. Any such impression would be misleading. It is basically a simple technique of netting-off reciprocal monetary obligations, even where there is no room for legal set-off, developed and used by masters in the Court of Chancery in giving directions for the administration of the estates of deceased persons. Complication arises only in a situation of insolvency, where the equitable rule produces a different outcome from that produced by statutory set-off.
>
> [41] In *Derham on the Law of Set-Off* (4th Ed, 2010, Oxford University Press), at [14.02], the learned author notes that the authorities have emphasised that that *Cherry v Boultbee* has a wider application than set-off, and rests upon quite different principles. As Swinfen-Eady J said in *Re Rhodesia Goldfields Ltd; Partridge v Rhodesia Goldfields Ltd* [1910] 1 Ch 239 at 246-247, the rule is of general application that where an estate is being administered by the Court, or where a fund is being distributed, a party cannot take anything out of the fund until he has made good what he owes to the fund. This is because it would be inequitable that a person entitled to a share of a fund should not receive anything in respect of that share without paying what he may be bound to contribute to the same fund.
>
> [42] The authorities also indicate that nothing is in strict language set-off; rather, the contributor is paid by holding in his own hand a part of the mass, which, if the mass were completed, he would receive back. The Court in effect says to the person claiming to be paid "you have in your hands that which is applicable to the payment – pay yourself out of that": *Re Rhodesia Goldfields* at 246, citing *In Re Goy & Co Ltd* [1900] 2 Ch 149 at 153 (Stirling J).
>
> [43] Consistent with the authorities referred to above, the principle is best described as a right to appropriate a particular asset as payment, as opposed to a right of set-off or a right of retainer: *Derham on the Law of Set-Off* at [14.03].

(See also Re D & D Corak Investments Pty Ltd (in Liquidation) [2020] NSWSC 1197 at [18] (Rees J).)

118 Accepting that the rule in *Cherry v Boultbee* requires a netting-off of reciprocal monetary obligations (*In Re Kaupthing Singer & Friedlander Ltd (In*

Administration [2011] UKSC 48; [2012] 1 AC 804 at [13]-[20]), the liquidator submitted that, strictly, the netting off does not occur at the stage of Lease Collateral's claim to prove as a priority creditor under s 556(1)(e), but occurs at the earlier and first stage of Lease Collateral's right to prove as a priority creditor under s 556(1)(c), and to the extent that Lease Collateral's obligations to contribute to the fund remains unsatisfied, the netting off then occurs at a second stage under s 556(1)(e). That is, Lease Collateral's liability to pay to Force Corp the amount of $546,563.81 is not (wholly) netted off against its right to prove as a priority creditor under s 556(1)(e) for $856,515.97 as the table reproduced at [9] above suggests. I accept that submission.

119 Three further matters should be noted. First, no problem arises with Lease Collateral participating as a priority creditor under s 556(1)(e) without having first contributed the whole of the amount of $546,563.81 to the fund available to the liquidators in the winding-up, for the benefit of other priority creditors since there are no priority creditors at the s 556(1)(c) level other than Lease Collateral.

120 Second, Lease Collateral is to be treated as having a right to appropriate its claim as a priority creditor under s 556(1)(c) in the amount of $315,442.97 as part payment of its liability to contribute $546,563.81 to Force Corp.

121 Third, Lease Collateral is also to be treated as having a right to appropriate its priority claims under s 556(1)(e) for $51,142.62 and $856,515.97 to the extent necessary as payment of the balance of its liability to contribute $231,120.84 to Force Corp ($546,563.81 less $315,442.97).

122 To give effect to the rule in *Cherry v Boultbee*, counsel for the liquidators proposed that a direction be given the following terms:

> The liquidators are entitled to direct Lease Collateral Pty Ltd to appropriate its liability to contribute $546,563.81 to Force Corp Pty Ltd in part satisfaction of its right to prove as a priority creditor of Force Corp Pty Ltd for the amounts of:
>
> (a) $315,442.97 (under subsection 556(1)(c) of the Act);

(b) $51,142.62 (under section 560 and subsection 556(1)(e) of the Act); and

(c) $856,515.97 (under subsection 556(1)(e) of the Act),

such that the amount payable to Lease Collateral Pty Ltd as a priority creditor in conformity with paragraphs 1, 2 and 3 above is $676,537.75.

123 Subject to some amendments to the terms of the direction, as indicated in the order below, it is appropriate that the Court give the liquidators a direction to this effect.

D. The LeasePLUS Payment Issue

124 *Corporations Act*, s 560 provides:

> **560 Advances for company to make priority payments in relation to employees**
>
> If:
>
> (a) a payment has been made by a company:
>
> (i) on account of wages; or
>
> (ii) on account of superannuation contributions (within the meaning of section 556); or
>
> (iii) in respect of leave of absence, or termination of employment, under an industrial instrument; and
>
> (b) the payment was made as a result of an advance of money by a person (whether before, on or after the relevant date) for the purpose of making the payment;
>
> then:
>
> (c) the person by whom the money was advanced has the same rights under this Chapter as a creditor of the company; and
>
> (d) subject to paragraph (e), the person by whom the money was advanced has, in the winding up of the company, the same right of priority of payment in respect of the money so advanced and paid as the person who received the payment would have had if the payment had not been made; and
>
> (e) the right of priority conferred by paragraph (d) is not to exceed the amount by which the sum in respect of which the person who received the payment would have been entitled to priority in the winding up has been diminished by reason of the payment.

125 The effect of s 560 is that if a payment has been made by a company on account of wages or superannuation contributions (whether before, or after, commencement of the external administration, here, the administration commencing on 13 July 2015) and the payment was made as a result of an advance of money made for that purpose, then the payor has the same right of priority in the winding up as the recipient of the money with respect to the money so advanced. The provision operates as a form of statutory subrogation.

126 Lease Collateral, Force Corp and the receivers entered into an agreement on 10 August 2015 described as a Short-Term Funding Agreement which contained the following provisions:

> 1. Force Corp hereby requests Leas Collateral to make available to Force Corp advances solely to fund payments by Force Corp of the kind described by s 560(a) of the *Corporations Act 2001* (Cth):
>
> (a) to LeasePLUS on account of unpaid employee wages comprising amounts owing under certain novated leases which form part of the salary package payable by Force Corp to employees (Outstanding Lease Payments) in an aggregate amount not exceeding $51,142.65 (or such greater amount that Lease Collateral in its absolute discretion agrees in writing) (Initial Advances) …
>
> 2. Lease Collateral agrees to provide each Initial Advance … subject to each condition set out in clause 9 (each a Condition) being satisfied or waived in writing as notified by Lease Collateral to Force Corp and this document [sic]
>
> …
>
> 6. Force Corp irrevocably and unconditionally directs Lease Collateral to arrange for the Initial Advances to be paid on behalf of Force Corp to LeasePLUS in satisfaction of the Outstanding Lease Payments.
>
> …
>
> 9. The Conditions are:
>
> (a) this document is duly executed by each party (other than Lease Collateral); and
>
> (b) evidence satisfactory to Lease Collateral that the EE Account [a separate account to be established and operated by Force Corp] has been established with a bank and on terms

(including as to account signatories) acceptable to Lease Collateral.

127 On 12 August 2015, Lease Collateral paid the amount of $51,142.65 to LeasePLUS with respect to amounts outstanding from Force Corp for certain of its employees under a salary packing arrangement with respect to novated leases for motor vehicles which formed part of the salary package of those employees which amounts were deducted by Force Corp for their wages on a monthly basis. Those leasing arrangements were provided by LeasePLUS Service Pty Ltd and on the commencement of the administration there were unpaid amounts owing to LeasePLUS under those novated leases by Force Corp. These amounts fall within the definition of "wages" in s 9 of the Act which include amounts payable to or in respect of an employee of the company under an industrial instrument, which includes a contract of employment, including amounts payable by way of allowance or reimbursement.

128 The question on which the liquidators seek a direction is whether the payment by Lease Collateral of $51,142.65 falls within s 560 of the *Corporations Act*, in circumstances where that amount was paid by directly to LeasePLUS, rather than the payment to LeasePLUS being made out of a Force Corp account. The reference in s 560(b) to an "advance" of money is to loan to the company, which creates a debtor-creditor relationship, as distinct from a gift or transfer to the company to be held on trust; *Lombe v Wagga Leagues Club Limited* [2006] NSWSC 3 at [27].

129 The liquidators point to the textual requirement in s 560 that the payment be made "by the company" and accept, correctly in my view, that this means that s 560(a) only applies where the company the subject of the winding up pays the employee / related liabilities itself, using monies lent to it by another person: *Re Dalma (No 1) Pty Ltd (in liq)* [2013] NSWSC 1335; (2013) 279 FLR 80 at [11] (Brereton J).

130 The Short-Term Funding Agreement involved the provision of a loan by Lease Collateral to Force Corp. The effect of the direction to pay in clause 6 is

that Lease Collateral, as lender, was directed by Force Corp, as borrower, to make payment of the sum of $51,142.65 direct to LeasePLUS. That payment answers the description in s 560(a) of a payment "made by a company" and the description in s 560(b) of a payment made as a result of an "advance" of money by a person for the purpose of making the payment. The payment had the effect of automatically discharging Force Corp's liability to LeasePLUS: *Burness v Supaproducts Pty Ltd* [2009] FCA 893; (2009) 259 ALR 339 at [44]-[45] (Gordon J).

131 The present case is distinguishable from *Re Dalma*, where Dalma Constructions paid the relevant liabilities to employees directly and contemporaneously wrote to the administrators of the company to the effect that it had made the payments and was seeking to rely on s 560. In *Re Dalma*, there was no payment made by direction of the company.

132 The liquidators properly drew the Court's attention to the possibility of a constructional choice that on a literal reading of the words "by a company" in s 560(a), the LeasePLUS payment does not fall within the terms of the provision. In my view, the effect of the provision is clear. Section 560(a) requires a payment "made by a company". A company makes a payment when it directs its lender to pay the advance to a third party "on account of wages".

133 A direction will be given that the liquidators would be justified in treating the LeasePLUS payment as falling within s 560 of the Act and accordingly, having the priority given under s 556(1)(e) of the Act.

Conclusion and Orders

134 The liquidators have made out a case for the directions they seek in the originating process, subject to amendment of the proposed direction in par [3] of the originating process to reflect the application of the rule in *Cherry v Boultbee*.

135 The liquidators seek an order that costs of the proceedings should be costs in the winding up of Force Corp. That order is appropriate. The liquidators submit that there should be no order as to the costs of Lease Collateral with the intent that it bears its own costs of the proceedings. Lease Collateral did not submit to the contrary.

136 Accordingly, the Court gives the following directions and makes the following order:

(1) A direction that the liquidators would be justified in treating the amount of $315,342.97 as being monies advanced by Lease Collateral Pty Ltd to the first plaintiffs, in their capacity as the then joint and several administrators of Force Corp Pty Ltd (Force Corp), for their remuneration and disbursements during the administration of Force Corp, and as a debt or claim falling within s 556(1)(c) of the *Corporations Act 2001* (Cth) (the Act).

(2) A direction that the liquidators would be justified in treating the amount of $51,142.62 as being monies advanced by Lease Collateral Pty Ltd to the receivers and managers of Force Corp and to Force Corp, for the purpose of Force Corp paying pre-appointment wage entitlements to employees of Force Corp, and as a debt or claim falling within ss 560 and 556(1)(e) of the Act.

(3) A direction that, subject to par 5 below, the liquidators would be justified in treating the amount of $856,515.97 as being monies paid by the receivers and managers of Force Corp to the employees of Force Corp out of the circulating assets of Force Corp, and as:

(a) having been paid in accordance with s 433(3)(c) of the Act; and

(b) a debt or claim falling within s 556(1)(e) of the Act.

(4) A direction that the liquidators would be justified in treating the amount of $546,563.81 as being monies realised by the receivers and managers of Force Corp, and as:

(a) having not been paid by the receivers and managers of Force Corp to the employees of Force Corp out of the circulating assets of Force Corp; and

(b) having not been paid in accordance with s 433(3)(c) of the Act.

(5) A direction that on the proper application of the rule in *Cherry v Boultbee* in the circumstances of the liquidation of Force Corp, the liquidators would be justified in directing Lease Collateral Pty Ltd to appropriate its liability to contribute $546,563.81 to Force Corp as follows:

(a) as to $315,442.97, in full satisfaction of its right to prove as a priority creditor of Force Corp for the amount of $315,442.97 (under subsection 556(1)(c) of the Act) in conformity with par [1] above;

(b) with respect to the balance of $231,120.84:

(i) as to $51,142.62, in full satisfaction of its right to prove as a priority creditor of Force Corp for the amount of $51,142.62 (under s 560 and subsec 556(1)(e) of the Act); and

(ii) as to the balance of $179,978.22, in part satisfaction of its right to prove as a priority creditor of Force Corp for the amount of $856,515.97 (under subsec 556(1)(e) of the Act),

such that the amount payable to Lease Collateral Pty Ltd as a priority creditor under s 556(1)(e) of the Act in conformity with pars [2] and [3] above is $676,537.75.

(6) Order that the costs of and incidental to the originating process shall be costs in the winding up of Force Corp Pty Ltd (in liq).

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