

Division 4A of the Bankruptcy Act (Cwlth) – worth a second look?

by Alison Umbers, Barrister

The purpose of Division 4A

Division 4A is designed to prevent a potential bankrupt from putting assets beyond the reach of a trustee in bankruptcy by channeling income to a family trust or other structure controlled by the bankrupt.

It is, essentially, a “claw back” provision, though not as well known as the other anti-avoidance provisions in the Bankruptcy Act such as s120 (undervalued transactions), s121 (transfers to defeat creditors) and s122 (avoidance of preferences).

The relief available under Division 4A

Where a trustee in bankruptcy successfully proves each of the elements required by s139D(1), the Court may order that the “controlled” property vests in the trustee in bankruptcy¹.

Alternatively, the Court may order the entity to pay the trustee an amount that represents the increase in the net worth of the value of the entity as a result of the services provided by the bankrupt (s139E).

Similar forms of relief are available where the entity is a natural person, pursuant to s139DA and s139EA.

The elements of a claim under s139D

The operation of s139D is limited to a relatively specific fact scenario, comprising of six elements, all of which must be met:

1. the bankrupt provided personal services to, or for or on behalf of, an entity (such as a family trust or company) (“the respondent entity”) during the examinable period as defined in s139CA;²
2. the bankrupt controlled the respondent entity at the time he or she provided the personal services³;
3. the bankrupt received no remuneration for the services, or the remuneration received by the bankrupt for the services was substantially less in value than a person in similar circumstances might reasonably be expected to have received in an arm’s length situation⁴;
4. the respondent entity acquired property as a direct or indirect result of the services provided by the bankrupt⁵; and
5. the bankrupt derived a benefit (whether directly or indirectly) from the property acquired by the respondent entity⁶; and
6. the respondent entity has an estate in the property at the time the trustee applies for recovery under Division 4A⁷.

In addition to the matters set out above, s139F(2) requires the Court to take into account any hardship an order might make to the respondent entity’s creditors.

Issues with s139D

Section 139D has been the subject of only a handful of reported decisions. This may be because the prospects of each of the six elements required by s139D presenting themselves before a

OAM Award

Congratulations to **Jim Cyngler**, one of our barristers who specializes in mediation and commercial law, on receiving a medal in the General Division of the Order of Australia in the recent Queens Birthday Honours list. Jim received the award for service to the community in the area of Jewish education.



Recent Seminar

Our recent seminar “Using nuclear weapons of the Law-Anton Piller orders & Mareva orders” presented by Peter Booth and Nick Jones and chaired by Rodney Garratt QC on the 26th March 2009 is available on our website at www.gordonandjackson.com.au

Keep your eye out for our next seminar in which Richard Boaden and John Salamanca will address issues arising from “The High Court & the Spry case” which will be held in mid August.

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bankrupt's trustee in a relatively uncomplicated fashion is about as likely as selecting six winning lotto numbers.

But, on a more serious note, assuming that the specific fact scenario contemplated by s139D can be made out, the relatively few cases in this area demonstrate that in addition to the threshold issue, there are also interpretation issues.

For example, in *Birdseye v Sheahan (2002) 196 ALR 598*, the bankrupt, Mr Birdseye, was an accountant who was the trustee of a trading family trust (the trust was "the respondent entity" for the purpose of s139D(1)).

Accounting fees generated by Mr Birdseye were paid to the family trust. The family trust paid Mr Birdseye \$15,000 per annum.

Mr Birdseye's wife used funds in the family trust bank account to make capital and interest payments due under a loan secured by a mortgage over the family property.

At the time this case was decided, s139D(1)(d) required the trustee to show, as one of the elements, that : *"the bankrupt used, or derived a benefit from the property at a time or times during the examinable period when the bankrupt controlled the entity in relation to the property"*

The Court held that even though Mr Birdseye lived in the house that was funded by the loan, he had not derived a benefit from the loan itself. There had to be a direct benefit from the loan in order to satisfy s139D(1)(d) (eg by the bankrupt using the loan as security).

Post Birdseye – 2006 amendment to s139D

The words "(whether directly or indirectly)" were inserted after the word "derived" in s139D(1)(d) as a result of Bankruptcy Legislation (Amendment) Anti-Avoidance Act 2006. Such an amendment overcomes the difficulties encountered by the trustee in the Birdseye decision. Though there are no reported decisions on s139D since its 2006 amendment, in cases where the threshold elements can be made out, this amendment is likely to extend the application of section 139D(1) for the benefit of trustees in bankruptcy and, ultimately, the creditors of bankrupt estates.

A short note on s139DA

Interestingly, cases on s139DA (also introduced in 2006 and which applies the general principles in s139D to natural persons) are also yet to emerge. The elements to be satisfied under section 139DA are similar to those under its s139D counterpart, but do not include the "control" requirement. Further, s139DA speaks of financial contributions rather than services, and there is no requirement relating to remuneration. Accordingly, s139DA may well be the more likely subject of future Division 4A litigation.

Alison Umbers practices in corporate and personal insolvency matters, and has acted for a number of trustees and liquidators before coming to the Bar in May 2009.

¹ Section 139(2). Further, the Court can appoint the Registrar to execute the necessary documents in the name of the controlled entity if necessary – see s139G

² s139D(1)(a)

³ s139D(1)(a)

⁴ s139D(1)(b)

⁵ s139D(1)(c)

⁶ s139D(1)(d)

⁷ s139D(1)(e)



When Reasons are Inadequate

– a commentary on the recent decisions of Justice Kyrou in *Sherlock v Lloyd [2008] VSC 450* and Justice Pagone in *Western Health v Gallichio & Ors [2009] VSC 134*.

A divergence of judicial opinion has emerged in recent cases involving opinions of medical panels constituted under the *Accident Compensation Act 1985* or under Part IVB of the *Wrongs Act 1958* as to whether inadequacy of the panel's reasons for a decision will be sufficient, in and of itself, to constitute an error of law or, at least, an error that allows the decision to be set aside in judicial review proceedings.

Medical panels are required to afford procedural fairness (or natural justice)¹ and to provide reasons for their opinions. The obligation to provide reasons arises by operation of section 8(1) of the *Administrative Law Act 1978* ("the ALA") as authoritatively construed in the decision of the Victorian Court of Appeal in *Masters v McCubbery*.² The reasons provided by a medical panel must be sufficient to enable the Court and the parties to see that the medical panel has arrived at its decision according to law; has addressed its mind to relevant matters; and has not acted unreasonably.³

Sherlock v Lloyd [2008] VSC 450 (29 October 2008) (“Sherlock”)

In *Sherlock*, the plaintiff alleged that she had suffered a recurrence of a depressive condition as a result of her employment as a payroll officer with the fourth defendant. In November 2007, seven medical questions were referred to the medical panel⁴ by a County Court Judge. The Plaintiff brought a proceeding for judicial review under Order 56 of the *Supreme Court (General Civil Procedure) Rules 2005* (“**Order 56**”) on the grounds, amongst others, that the reasons of the medical panel were inadequate.

Justice Kyrou concluded that the reasons provided by the medical panel failed to enable the Court or the parties to understand how the panel had reached its conclusions and were inadequate.⁵ His Honour held, however, that the inadequacy of the reasons was insufficient, in itself, to justify an order quashing the medical panel's opinion.⁶ His Honour stated that:⁷

- ▶ as the legal obligation to provide reasons arises under section 8 of the ALA, the remedies for inadequate reasons must be determined solely by reference to the statutory remedies contained in that section;
- ▶ the remedy provided by section 8(4) of the ALA for inadequate reasons provided pursuant to s8(1) of the ALA is an order for a further statement of reasons;
- ▶ it is only if that subsequent order for the provision of reasons is not complied with, or if the reasons subsequently provided are inadequate, that the Court may quash the decision of the panel under section 8(4) of the ALA “*as if error of law had appeared on the face of the record*”; and
- ▶ accordingly, where an applicant seeks to complain about the adequacy of reasons given by a tribunal (such as the medical panel) under section 8 of the ALA, that may be done only by making an application under section 3 of the ALA⁸ or an application for a further statement of reasons under section 8(4) of the ALA. In both cases the only relief that the Court may give in respect of the inadequate reasons is the relief contained in section 8(4) of the ALA. In contrast, where an application for judicial review is brought under Order 56, no relief will be available where the complaint is solely that the tribunal's reasons are inadequate.

In reaching his decision Justice Kyrou rejected the decision of Smith J in *Pyle v Nissell*⁹ (“**Pyle**”) to the effect that inadequacy of reasons may constitute error of law sufficient to justify an order in the nature of certiorari (the quashing of the decision). The decision in *Pyle* has, since 2000, been taken by judges in the trial division of the Supreme Court to correctly state the law.¹⁰

Western Health v Gallichio [2009] VSC 134 (8 April 2009) (“Gallichio”)

The approach of Justice Kyrou J on this issue was promptly rejected by Pagone J in *Gallichio*. There the plaintiff challenged the determination of the medical panel on the grounds, amongst others, that the reasons it had provided were inadequate to discharge its legal obligation to provide reasons. Justice Pagone upheld that complaint.¹¹ In considering the consequences of that finding his Honour reviewed Kyrou J's analysis of section 8 of the ALA, concluding that:

- ▶ the general purpose of the obligation to provide reasons under section 8(1) of the ALA suggests that it was not intended to provide an exclusive code;¹² and
- ▶ accordingly, the specific remedy in section 8(4) of the ALA should not be considered to be the sole remedy available for a failure to comply with section 8(1), or to prohibit a Court from quashing a decision of a tribunal where its reasons are inadequate - regardless of whether the application for judicial review is made under the ALA or under Order 56.¹³

Practical implications of Sherlock

The decision of Kyrou J in *Sherlock* has created considerable uncertainty for practitioners dealing with decisions of tribunals who are subject to the obligation to provide reasons under section 8(1) of the ALA. On 20 February 2009, the Court of Appeal granted leave to the plaintiff to appeal *Sherlock*.¹⁴ In the meantime, it appears that applicants seeking redress for inadequate reasons may have greater certainty as to the available remedies where an application is brought under the ALA, rather than under the usual Order 56 procedure.

Meredith Schilling practices in commercial, taxation and administrative law and has appeared in judicial review proceedings involving decisions of medical panels: for example, *Campbell v Adlard and Ors* [2008] VSC 349.

¹ *Masters v McCubbery* [1996] 1 VR 635, 650-651 per Winneke P, 653 per Ormiston J and 661 per Callaway JA.

² *Ibid.*

³ *Ibid.*; see further, *Clarke v National Mutual Life Insurance Ltd* [2007] VSC 341 (Unreported, Forrest J, 18 September 2007) at [43]; *Kamener v Griffin* (2005) 12 VR 192 at 204 (Ashley J); *Davidson v Fish* [2008] VSC 32 (Unreported, Pagone J, 18 February 2008) at [12]; *Robert Bosch (Australia) Pty Ltd v Barton* [2008] VSC 227 (Unreported, Judd J, 27 June 2008) at [24]; *Treacy v Newlands* [2008] VSC 395 (Unreported, Beach J, 2 October 2008) at [7]; *Sherlock v Lloyds* [2008] VSC 450 (Unreported, Kyrou J, 29 October 2008) at [39].

⁴ Pursuant to s45(1)(b) of the *Accident Compensation Act 1985*.

⁵ At [41]-[45].

⁶ At [46].

⁷ *Sherlock* at [20] to [25]; [35].

⁸ Section 3 of the ALA provides, in summary, that any person affected by a decision of a tribunal may make application to the Supreme Court for an order calling on the tribunal, its members or any interested party to show cause why the decision should not be reviewed.

⁹ [2000] VSC 398

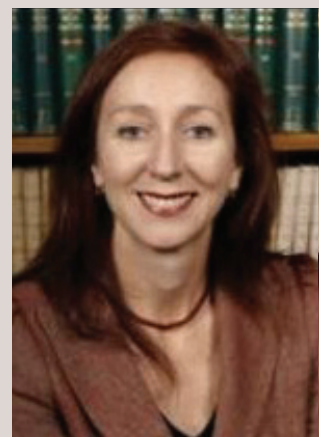
¹⁰ This fact was noted by Kyrou J at para [31].

¹¹ At [15].

¹² At [22]; see also Gobbo J's reasoning in *State Electricity Commissioner v Commissioner for Equal Opportunity* [1992] 1 VR 79 at [86] to [89].

¹³ At [22]-[23].

¹⁴ It is anticipated that the appeal will not be heard until late 2009 or perhaps 2010.



A welcome to the new List Members

The following signed the Bar Roll on 21st May 2009



Alexandra Golding LL.B. [Univ. Adelaide]; B.Eco; Graduate Diploma in Legal Practice (SAIT)

Alex has practised as a solicitor for 20 years, most recently as a senior consultant at Moray & Agnew. She practises in the commercial sphere with particular interest in professional negligence, liability, environmental and building claims. She was seconded to a financial institution and undertook asset recovery work for that institution. She is experienced in all forms of ADR, particularly mediation. Alex is the current president of the Victorian chapter of the Australian Professional Indemnity Group and is also on the National Committee.



Simon Loftus LL.B: B.Comm.

Prior to coming to the bar, Simon spent three years as Senior Legal Counsel at Symbion Health Limited (subsequently Primary Health Care Limited.) Before that, Simon was a solicitor in private practice for 16 years with senior roles at DLA Phillips Fox, Herbert Geer and partnership at Ligeti Partners. During his time at Symbion Health, Simon was responsible for litigation and advice involving corporations law, contracts, trade practices, intellectual property, insolvency, product recall, privacy, the Health Insurance Act, occupational health and safety, insurance and medical negligence. Simon has a particular interest in health law matters. Simon's experience in private practice was exclusively in litigation acting for corporations and insurers in litigation involving contract and commercial disputes, insolvency, professional indemnity (including medical negligence), construction law and public liability.



Alison Umbers LL.B; B.Comm.

Alison was formerly a principal of Harwood Andrews Lawyers. She has practiced in commercial litigation since her admission in 1996, and has practiced in a wide range of commercial disputes representing banks, financiers, private lenders, insurers, insolvency practitioners and family businesses. She has a particular interest in the area of corporate insolvency and bankruptcy. The Law Institute of Victoria accredited Alison as a specialist in commercial litigation in 2004 and since that time Alison has been a member of the Law Institute's Commercial Litigation Advisory Committee. Alison is also a member of the Insolvency Practitioners Association of Australia.

Julian G. Ireland LLB has recently joined us from Hyland's List.

Julian practices in the areas of construction law, employment law, shipping and transport law, commercial law and all areas of common law. He is an accredited mediator (LEADR) and views mediation as a most cost effective dispute resolution forum. Julian is also a Sessional Mediator with VCAT and the Office of Small Business Commissioner. Julian is accredited by the Victorian Bar as an Advanced Mediator.

In 1996 Julian was appointed as a part time mediator to the Domestic Building Tribunal and was elected to the Committee of Mediators of that body. In 1997 he was appointed as assistant examiner in law by Deakin University. He is also a part time lecturer with the Detective Training School (Victoria) and Deakin University.

Julian is a member of the VCAT Mediators Committee and Mediates in the Domestic Building List, Retail Tenancy List and Real Property List. He is also a Mediator for the Small Business Commissioner. He holds appointments to the Commonwealth Franchisees Mediation Panel as well as the Produce and Grocery Panel.

Julian is on the Bar A.D.R. Committee.



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