IN THE HIGH COURT OF AUSTRALIA
MELBOURNE OFFICE OF THE REGISTRY

141
No. M 81 of 2013

BETWEEN

JAMES HENRY STEWART in his capacity as liquidator of NEWTRONICS PTY LTD (in liquidation)
First Appellant

10 **NEWTRONICS PTY LTD** (receivers and managers appointed) (in liquidation) (ACN 061 493 516)
Second Appellant

and

ATCO CONTROLS PTY LTD (in liquidation) (ACN 005 182 481)
Respondent

APPELLANTS' REPLY

1. On the submissions, five key issues emerge as the battle ground between the parties. First, *are the conditions for the equitable lien for a liquidator established?* Has the secured creditor come in under the liquidation or otherwise become beholden to the
20 liquidator such that Equity requires the secured creditor to acknowledge the liquidator's expense and effort in preserving and realising the asset which the secured creditor now claims?

2. Consistently with the cases examined by Sir Owen Dixon, the lien applies because the secured creditor here has not itself realised the asset under its security or in proceedings which it brought; the asset was the product of the liquidator's exertions in pursuance of his duty to get in assets of Newtronics for the benefit of those creditors entitled to them and in the exercise of his powers as liquidator; the asset having been realised in that way, the secured creditor came into the liquidation when and by the fact that it claimed the asset after settlement of the liquidator's proceedings, and, to pursue its claim, it brought
30 an appeal in the liquidation, under s 1321 of the Corporations Act.[1]

3. Secondly, *is there a special class of exceptions to a liquidator's equitable lien*, being where the occasion for the liquidator's action in preserving or realising an asset claimed by the secured creditor happens to be a proceeding brought against the secured creditor by the liquidator, including a suit to challenge the security? No rationale has been advanced to justify disapplication of the usual rule that the liquidator, having by court proceedings brought in $1.25 million to which the secured creditor is entitled, is entitled to a lien for the costs, expenses and reasonable remuneration exclusively incurred in the realisation of that sum. No case holds that secured creditors are immune from suit or

immune from the lien. The Respondent has not shown why the usual rule should not apply.

4. *Re M C Bacon Ltd* [1991] Ch 127 establishes no rule that proceedings by a liquidator against a secured creditor preclude the lien or are unjust per se (RS [44]). That was not a claim for an equitable lien: the liquidator had not realised any asset; he claimed under statute costs out of funds already in the hands of the secured creditor, to which the liquidator had not contributed. There was no reference to the authorities and principle underlying *Universal Distributing*. The case is peculiar to its own facts and statute.

5. Thirdly, *what is the nature of the 'benefit' to the secured creditor* conferred by the liquidator's action which justifies the liquidator's equitable lien taking priority to the creditor's security? Is it a net benefit after all costs; is it affected by whether there was a subjective intention to confer a benefit; is the possibility of benefit sufficient? Reference to taking the "benefit of the action" is deeply rooted in the nineteenth century equity cases (Appellants' Submissions [41], [42]). It has no connection with "incontrovertible benefit" of restitution (AS [57]). Authority makes clear that, where a sum has actually been realised and is claimed by the secured creditor, that is sufficient 'benefit': *Westpac Banking Corporation v ITS Taxation Services* (2004) 22 ACLC 229 at 235[27]:

> "The fact that the fund is unlikely to be adequate to meet the chargeholder's claims, after [the controller's] costs and disbursements are deducted, is not a ground for denying [the controller's] claims, for a receiver does not guarantee that his or her efforts will generate or preserve sufficient assets to meet all creditors' claims. The fact that Mr Singleton's claim is in an amount not very different from the value of the assets he recovered during his receivership is coincidental and beside the point. *The chargeholders have had the benefit of Mr Singleton's efforts in the sense that he has preserved and augmented an asset of the company which will be available (subject to deduction of his costs and expenses) to meet all relevant claims including theirs.*" (emphasis added). This is what the liquidator has done in this case.

6. No authority supports the lien being qualified because of costs and expenses of the secured creditor, antecedent or ancillary to the fund being realised. Those matters are just as immaterial to the lien as the fact that the realised fund is insufficient to meet the secured creditor's claim after deduction of fees and expenses: "*even if the fund is insufficient to pay both the just costs of realisation of the receiver, and the debt owed to the debenture holder, the receiver is entitled to deduct and retain his moneys first.*" [2]

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[1] Additionally, it initiated a complaint "with respect to the conduct of the liquidator in connection with the performance of his duties" under s 536(1)(b) of the Corporations Act.

[2] *Moodemere Pty Ltd v Waters* [1988] VR 215 at 221, pointing out that *Universal Distributing* was such a case.

7. This is the answer to the assertion that 'had the work [of the liquidator in bringing the promise of support proceeding] not been done, Atco would have been better off' (CA at [77], [223], 295]). That asks the wrong question and looks at the wrong factors. The correct approach is to say that had the work of the liquidator not been done, Atco would not have available to it (subject to deduction of costs and expenses) $1.25 million.

8. Contrary to the Notice of Contention, the subjective intent of the liquidator should not be determinative; the lien should apply to the costs of realizing a particular fund if objectively the liquidator's work produced it.[3] The liquidator is statutorily directed to act, and should be assumed to be acting, for the benefit of creditors.[4] The outcome, not the subjective motivation for the bringing of the proceedings, is the test, as shown by *Batten, Proffitt & Scott v Dartmouth Harbour Commissioners* (1890) 45 Ch D 612. In that case, the junior encumbrancer had attacked the senior debenture holder's security. Nevertheless, the outcome conferred actual benefits on the senior creditors and a lien was allowed. This was entirely consistent with *Wright v Kirby* (1857) 23 Beav 463; 52 ER 182: AS [42] and other cases in which the proceedings would have had to be brought in any event.[5] In *Dartmouth Harbour*, all that occurred was that the expenses given priority under the lien were limited to exclude "some of the costs ... incurred on their own behalf only". That is a case about the directness of the relationship of expenses to the outcome generated, not about denial of the lien because there was an attack on the secured creditor's security. The lien covers all expenses that "are reasonably incurred in the care, preservation and realisation of the property" (*Re Universal Distributing* at 174). Remuneration for work directed to the exclusive purpose of raising the fund may also be claimed (at 175). These are factual enquiries about the connection between expense and outcome (see cases on the equivalent test in s 564[6]). The respondent accepts that the "settlement sum was produced by the claim against the receivers": RS [80]. That admission defeats the Notice of Contention.

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[3] The costs and expenses that have priority pursuant to the equitable lien "are assessed by reference to actual events and the actual costs of the person who realises the fund. ... The limitation on whether the actual expenses incurred are to be given priority is whether they were reasonably incurred": *Meadow Springs Fairway Resort Ltd v Balanced Securities Ltd* (2008) 65 ACSR 563 at 586 [135], drawing on *Batten v Wedgwood Coal and Iron Co (No 1)* (1884) 28 Ch D 317 at 325.

[4] *Bertrand v Davies* (1862) 31 Beav 429 at 436; 54 ER 1204 at 1207; *Shirlaw v Taylor* (1991) 31 FCR 222 at 230. No complaint has been made against the liquidator or any finding made that the proceedings were not warranted.

[5] *In re Regent's Canal; Ex parte Grissell* (1875) 3 Ch D 411, 427; *Batten v Wedgwood Coal and Iron Co* (1884) 28 Ch D 317, 325; *Re Universal Distributing Co* (1933) 48 CLR at 174.9.

[6] *Re Kyra Nominees* (1987) 11 ACLR 767; *DCT v Currockbilly* (2003) 21 ACLC 136; *Tolcher v National Australia Bank* (2004) 48 ACSR 741.

9. Fourthly, *has the lien been displaced or waived* by the terms of the indemnity between indemnifying creditor and liquidator? Has anything in the liquidator's conduct precluded the lien arising? In the indemnity agreement, the liquidator agreed on request to seek an order under s 564 to secure priority to the secured creditor out of recoveries. The contractual reference to the statute is capable of coexisting with the equitable lien, in the same way that the equitable lien coexists with various statutory liens for controllers: see *Shirlaw v Taylor* (1991) 31 FCR 222 at 231-232; *Weston v Carling Constructions Pty Ltd* (2000) 35 ACSR 100 at 104 [18]; *ASIC v John McKenney Consulting* (2002) 43 ACSR 458 at 466-468 [32]-[36], [41]; *Coad v Wellness Pursuit Pty Ltd* (2009) 40 WAR 53. On an objective reading of the agreements, nothing excludes recourse to the lien.

10. Further, none of the conduct of the liquidator before or after entry into the agreements constitutes a waiver of the lien or of the liquidator's obligation under a contract of indemnity to account to the indemnifier out of any recoveries: AS [68]. When the liquidator sought approval nunc pro tunc to enter into the indemnity agreements, the issue was whether the funder was being given a benefit disproportionate to the risk undertaken or a "grossly excessive profit". In that context, reference to a future application under s 564 was to the funder relying on s 564 for any uplifted return. So understood, this is no waiver of the lien for recovery of costs incurred.

11. The principal use of section 564 is to provide funding creditors with a disproportionate share of net (post-costs) recoveries, as a variant of the pari passu principle. With respect to costs associated with recoveries, although encompassed by the wording of the section, no authority of the Court is required for the liquidator to take his costs out of the recoveries or for an indemnifying funder to recoup from the liquidator the costs and expenses so recovered which the funder had previously provided to the liquidator. There are numerous cases where costs of recovery in a liquidation are first reimbursed pursuant to a lien before the balance is distributed pursuant to an application under s 564: including *Re Kyra Nominees Pty Ltd* (1987) 11 ACLR 767 at 768-769, 777; *Household Financial Services Pty Ltd v Chase Medical Centre Pty Ltd* (1995) 18 ACSR 294, 296, 298; *Jarbin Pty Ltd v Clutha Ltd* (2004) 208 ALR 242; *Australian Steel Co (Operations) Pty Ltd v EPS Group Pty Ltd* (2006) 59 ACSR 602.[7]

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[7] In that case, out of settlement proceeds, the liquidator first reimbursed the funding provided under a putative deed of indemnity and paid other costs of realisation: at [32]. A separate application was made under s 564 for priority distribution of the net proceeds, pursuant to a clause in the deed requiring the liquidator to make an application under s 564 for priority in respect of any recoveries (that is, a clause to the same effect as those in this case): at [15]. No issue was taken that the repayment of the funder's

12. Indeed, so entrenched is the rule that costs of recovery are always allowed first, "*the authorities [on sec 564] do not reveal any examples of an advantage being conferred upon an indemnifying creditor in priority to the costs of recovery of the property*": *Deputy Commissioner of Taxation v Vintage Gold Investments Pty Ltd* [2009] FCA 967 per Greenwood J at [40]. Against this background, the reference to an application under s 564 is of no consequence or effect on the lien or the obligation to account to the indemnifier.

13. Finally, *whether a unified theory of equitable liens has been or can be posited.* In *Hewett v Court* (1983) 149 CLR 639 the Court has confirmed that it is not possible (or necessary) to explain all equitable liens by a single test (per Gibbs CJ at 149 CLR 645-646; per Deane J at 667-668). Discussion of equitable liens in those passages and in such works as *Pomeroy's Equity Jurisprudence* are by way of general overview and introduction. They do no more than usefully describe the range of occasions in which a lien may be imposed, but the description does not displace the more detailed tests and rules that apply in different cases. The respondent seeks to determine the equitable lien by reference to "a subjective evaluation of what is unfair or unconscionable", when the correct principle is that the lien depends on "the existence of a qualifying factor falling into some particular category" recognised by authority (to adapt *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89 at 156; cf *Roxborough v Rothmans of Pall Mall Australia Ltd* (2001) 208 CLR 516 at 545; *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221 at 256). Accordingly, the answer to whether the "owner would be acting unconscientiously or unfairly were he to dispose of the property ... without the relevant liability having been discharged" lies in *Re Universal Distributing* and cases which deal specifically with the claims to a lien by a liquidator or other controller.

14. The U S cases cited by the Respondent's Submissions ([61] – [65]) confirm that from a common origin with Anglo-Australian law, US bankruptcy practice has developed liquidation-specific rules for recoupment by a controller of its costs and expenses in preserving or disposing of secured assets that are recognisable in part, but with differences in detail which it is not necessary to explore.

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contribution or payment of the liquidator's costs out of the realised sum was contrary to this term of the deed of indemnity or impermissible under s 564.

Dated: 14 February 2014.

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