HIGH COURT OF AUSTRALIA

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Details of Filing

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IN THE HIGH COURT OF AUSTRALIA

BRISBANE REGISTRY No. B19/2022

BETWEEN:

METAL MANUFACTURERS PTY LTD

(ACN 003 762 641)

Appellant

and

GAVIN MORTON as liquidator of MJ WOODMAN ELECTRICAL CONTRACTORS PTY LTD (IN LIQUIDATION)

(ACN 602 067 863)

First Respondent

MJ WOODMAN ELECTRICAL CONTRACTORS PTY LTD (IN LIQUIDATION)

(ACN 602 067 863)

Second Respondent

APPELLANT'S SUBMISSIONS

PART I: CERTIFICATION

1. This submission is in a form suitable for publication on the internet.

PART II: ISSUES ON APPEAL

2. This appeal, at its narrowest, concerns the issue of statutory construction whether the statutory set-off contained within s 553C of the *Corporations Act 2001* (Cth) (**Corporations Act**) has application in the context of a liquidator's claim for the recovery of an unfair preference under Part 5.7B of the Corporations Act, where there is a separate debt involved. In the proceedings below, the question reserved by Derrington J for consideration by the Full Court of the Federal Court was as follows:

> Is statutory set-off, under s 553C(1) of the Act, available to the defendant in this proceeding against the plaintiff's claim as liquidator for the recovery of an unfair preference under s 588FA of the Act? (Emphasis added)

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3. The Full Court answered this question in the negative. By this appeal, the appellant contends that the question ought to have been answered "yes". In reaching that answer it is appropriate, contrary to the view of the Full Court, to consider the interaction between s 553C and other recovery provisions (see [31]-[38] below).

PART III: SECTION 78B OF THE *JUDICIARY ACT 1903* (CTH)

4. The appellant has considered whether any notice should be given in compliance with s 78B of the *Judiciary Act 1903* (Cth). No such notice is required.

PART IV: THE JUDGMENT BELOW

5. The decision of the Full Court of the Federal Court was published with the following medium-neutral citation: *Morton as Liquidator of MJ Woodman Electrical Contractors Pty Ltd v Metal Manufactures Pty Limited* [2021] FCAFC 228 (**J**).

PART V: RELEVANT FACTS

6. The material facts for the purpose of this appeal are contained within the Statement of Facts in the Amended Special Case, contained at Core Appeal Book (**CAB**) at **6-8**, of which 3 matters are of note. **First**, the debt which the appellant seeks to set-off is separate and distinct from the debt which was the subject of the payment by the second respondent to the appellant (**CAB:7** [12A]). **Secondly**, the respondents concede that s 553C(2) does not apply on the facts of this case, which would otherwise preclude the appellant's reliance upon the set-off under s 553C(1) (**CAB:7** [11]). **Thirdly**, as the respondents' claim is yet to be litigated below, the appellant's pleaded defences (including under s 588FG) are undetermined.

PART VI: ARGUMENT

The Legislative Framework

7. As a matter of statutory interpretation, the starting point in the Court's analysis must be an examination of the text of the provision itself.[1] Historic experience (whether domestic or foreign), secondary and extrinsic materials, and *a priori* assumptions as to policy objectives cannot displace the clear meaning of the text.[2] Nor is it legitimate to

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1 *Alcan (NT) Alumina Pty Ltd v Commissioner of Territory Revenue* (2009) 239 CLR 27 at 46-7.
2 *Alcan (NT) Alumina Pty Ltd v Commissioner of Territory Revenue* (2009) 239 CLR 27 at 46-7.

pursue an identified legislative purpose to its farthest reaches in distortion of the enactment.[3]

The Starting Point: The Text of Section 553C of the Corporations Act

8. Section 553C(1) of the Corporations Act provides that a statutory set-off will apply where there are *"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 that company. An account is then taken pursuant to s 553C(1)(a) to determine what, in monetary terms, is owed by each party *"in respect of those dealings"*. In the case of an unfair preference claim advanced against a creditor, and a creditor's separate and distinct claim advanced against the company (i.e. in the absence of "circularity"),[4] the operation of s 553C is a simple one. Its work in the present case can be illustrated as follows:

   a. **First**, mutual dealings between the appellant (as vendor) and the second respondent (as purchaser) are identifiable as existing prior to the winding up. Those dealings comprised the supply of goods, the incurring of payment obligations, and the making of actual payments between the parties. The set-off under s 553C(1) is enlivened.

   b. **Second**, s 553C(1)(a) then requires that an account be taken of what is due from one party to the other in respect of those mutual dealings. In this case, the sum due from the company to the appellant is admitted in the sum of $194,727.23 (**CAB:7** [8]). On the other side of this account, the sum of $190,000 (representing the alleged preferential payment) belongs to the company and must be repaid by the appellant, forming the basis of the company's competing and off-setting claim.

   c. **Third**, by operation of s 553C(1)(b), the two sums within the account above are set-off against each other (there being no circularity). In the present case, the additional safeguard in favour of the company under s 553C(2) does not apply, nor does any overriding provision under as s 553A operate to disqualify the type of debt from the beneficial operation of s 553C. The result

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[3] *Certain Lloyd's Underwriters v Cross* (2012) 248 CLR 378 at 390.

[4] The appellant accepts that the answer to the question under appeal would be different in the case of a creditor seeking to set-off the very debt the payment of which gave rise to the unfair preference. This appeal does not concern the availability of a set-off involving such circularity. See also **J**[31].

is that, pursuant to s 553C(1)(c), the balance of $4,727.23 is admissible to proof by the appellant in the winding up of the company.

9. The Full Court criticises this result as *"arbitrary"* (**J**[156]) and one that *"offends the notion of fairness that underpins mutuality in s 553C"* (at **J**[155]). There are several difficulties in the Full Court's appeal to normative concepts of *"fairness"*. Most obviously, such concepts tend to obscure, rather than shed light upon, the enquiry as to the operation of s 553C. In addition, the *"fairness"* (and kindred concepts of *"equity being equality"* as an *"underpinning value"* (**J**[109])) are signposts capable of pointing in different directions. For instance, it is true that the object of Part 5.7B, expressed at its most general, is one of fairness,[5] but that merely begs the question as to what fairness dictates in a given circumstance. That question is not answered by invoking the *pari passu* principle (**J**[28]-[29]), for at least two reasons: **First**, the principle of *pari passu* is not absolute, being a principle to which Parliament has provided a number of exceptions.[6] There is no principled reason why, in light of the existence of other exceptions created by the legislature, s 553C should be decried as constituting an impermissible further exception to the *pari passu* principle. **Secondly**, the view that set-off constitutes an exception to the *pari passu* principle (a view embraced by the Full Court) is doubtful. It is possible to instead regard set-off as a form of equity attaching to the claim of the company in liquidation, such that it is only the balance which remains after the satisfaction of that equity that is subject to the *pari passu* principle.[7]

10. The Full Court's recourse to concepts of *"fairness"* and *pari passu* reflects its distaste for a conclusion that *"[i]f the statute so applies so be it"*. But that can provide no justification for a departure from the command of the statute; the *"surest guide to legislative intention is the text of the legislation itself"*.[8]

The Text in Context – The Structure of the Corporations Act

11. Aside from the text of s 553C itself, a number of observations concerning the Corporations Act can be seen to support the operation at paragraph [8] above.

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5 *BP Australia Ltd v Brown* (2003) 58 NSWLR 233 at [98] (Spigelman CJ).

6 See, for example: Corporations Act, ss 556, 558, 562, 562A, 563, 563AA, 563A.

7 R.M. Goode, *Principles of Corporate Insolvency Law* (Sweet & Maxwell, 1st Ed, 1990), at 68 (n 33).

8 *Hilder v Dexter* [1902] AC 474 at 477-478 (Earl of Halsbury LC), cited in *Alcan (NT) Alumina Pty Ltd v Commissioner of Territory Revenue* (2009) 239 CLR 27 at 46-7.

12. **First**, the Corporations Act does not contain any provision which excludes s 553C from operating in respect of the unfair preference regime (or any other recovery provision within Part 5.7B), nor does the text of s 553C admit of such a limitation. Parliament was expressly invited by the Australian Law Reform Commission to enact further limitations upon the operation of s 553C, but declined to do so.[9]

13. **Secondly**, there is nothing in the *structure* of the Corporations Act which tells against the application of s 553C. The unfair preference regime is contained within Part 5.7B of the Corporations Act, whereas s 553C is located within Part 5.6. The Full Court correctly observed (at **J**[108]) that these two parts do not have *"different spheres of operation"* as had been earlier submitted by the respondents.

14. **Thirdly**, the presence of s 588FI does not detract from the application of s 553C in the context of unfair preferences (*c.f.* **J**[133]). That section enables a creditor, after disgorging a preference under s 588FF, to participate in the winding up by proving for the amount disgorged. The operation of the set-off under s 553C does not alter or frustrate the operation of s 588FI. Take the following example. Let it be supposed that a creditor receives a preferential payment of $100, whilst being owed $75 by the company as a separate and distinct debt. The account required by s 553C(1)(a) results in the creditor being liable to repay to the company the sum of $25, being the balance after set-off. Once repaid, s 588FI permits the creditor to prove in the winding up in respect of the $25. Nothing in this process gives rise to any conflict or incoherence in the operation of the two provisions; the Full Court's view that they sit *"incongruously and uncomfortably"* (**J**[135]) is incorrect.

Ground 1 - The Mutuality Requirement

15. The Full Court's principal reason for rejecting the application of s 553C in the context of unfair preference recovery, was the asserted lack of mutuality (**J**[7]). The absence of this mutuality was said to exist on two levels: **First**, the distinction in the nature of the interest in which the company owes money to the creditor on the one hand, and the interest in which a creditor owes money to a company through the recovery of an unfair preference on the other.

16. **Secondly**, the absence as at the relevant date of any right or equity (vested or contingent) in the company or duty or obligation (vested or contingent) in the creditor

[9] See: [39]-[42] below.

to recover or to repay the preference respectively (**J**[7]). Both of these holdings by the Full Court were erroneous.

The "Three Aspects" to the Requirement for Mutuality

17. Before turning to the Full Court, it is necessary to give content to the expression "mutuality" as applying in the context of set-off. The concept has been explored by this Court in three principal decisions: ***Hiley*** *v People's Prudential Assurance Co Ltd* (1938) 60 CLR 468; ***Day & Dent*** *Constructions Pty Ltd v North Australian Properties Pty Ltd* (1982) 150 CLR 85 and ***Gye v McIntyre*** (1991) 171 CLR 609.

18. *Hiley* involved a liquidator's action to set aside certain transfers of mortgages by the appellant. The appellant asserted a set off in respect of damages against the company for repudiating the policies of insurance granted. A question arose whether the bank's claim to avoid the transfers of mortgage was a contingent claim attracting the set-off provision under bankruptcy legislation. The majority held that it was sufficiently contingent,[10] with Dixon J explaining (at 497) (emphasis added):

> It was enough that at the date of the commencement of the winding up mutual dealings exist which involve rights and obligations whether absolute or contingent of such a nature that afterwards in the events that happen they mature or develop into pecuniary demands capable of set off. [11]

19. Although no action had been propounded, his Honour found that the elements *"upon which it was afterwards based existed at the time when the winding up commenced"* (at 498). As is explored at [27]-[38] below, there is parallel in such a conclusion and the existence of the unfair preference recovery commenced in winding up.

20. In *Day & Dent,* the Court likewise emphasised the width of the concept of mutuality in the context of set-off. The case concerned a debt of $100,000 owed by a company "NAP" to Day & Dent (in liquidation). After the commencement of the winding up, NAP had paid a debt owed by Day & Dent as surety under a guarantee. NAP sought to set-off its debt to Day & Dent against its claim against Day & Dent for recoupment arising from its payment as surety. As the liability of Day & Dent to NAP, arose after the commencement of the winding up, the question was whether there was sufficient mutuality at the relevant date. Gibbs CJ (at 91), citing *Hiley* as governing, observed

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[10] Rich, Stark and Dixon JJ; Latham CJ dissenting.

[11] Emphasis added.

that it was enough that, as at the relevant date, there *"existed on one hand a debt and on the other hand a liability which in due course might mature into a debt"*.[12] In agreeing in this result, Mason J observed (at 108) that it was reasonable to *"impute to Parliament an intention that the provision, which is a protective provision, be given the 'widest possible scope'"*.[13]

21. More recently, in *Gye v McIntyre*, whilst considering the equivalent set off provision under s 86 of the *Bankruptcy Act 1966* (Cth) (**Bankruptcy Act**), the Court observed (at 618-9) that a statutory set-off provision is intended to effect *"substantial justice"* between the parties. The Court observed by reference to *Day & Dent*, that provisions *"such as s.86"* should be given *"the widest possible scope"*.[14] The Court proceeded to hold (at 623) that the mutuality requirement under s 86 of the Bankruptcy Act involved *"three aspects"*: (a) that the credits, debts or claims arising from other dealings be between the same person; (b) that the benefit or burden of them lie in the same interests, for which purpose it *"is the equitable or beneficial interests of the parties which must be considered"*; and (c) that they ultimately sound in money.[15]

The Full Court's First Core Holding: Mutuality of Interest (Beneficial Entitlement)

22. The Full Court concluded (at **J**[151]) that the appellant and the second respondent did not assert competing claims *"in the same interest"* for the purpose of mutuality. That conclusion is erroneous and the product of an unduly restrictive interpretation of the mutuality requirement; placing a restrictive gloss on the text of s 553C which ought instead be given the *"widest possible scope"*.

23. The Full Court's analysis begins with the critical observation (at **J**[143]) that the requirement of mutuality of interest is satisfied only *"in point of relevant beneficial entitlement"*, citing in aid of that observation *Hiley* and *Gye v McIntyre*. Contrary to this foundational observation by the Full Court, neither *Hiley* nor *Gye v McIntyre*[16] support the proposition that, for mutuality of interest to exist, the parties must not only possess claims involving competing beneficial interests, but that such interests must be a *"relevant"* beneficial interest. The addition of a relevance qualification to the second aspect of mutuality described by the Court in *Gye v McIntyre* (at 623) is a gloss

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[12] Emphasis added; also citing *Sovereign Life Assurance Co v Dodd* [1892] 1 QB 405 at 411-412.
[13] Citing *Eberle's Hotels and Restaurant Co v Jonas* (1887) 18 QB 459 at 465.
[14] *Gye v McIntyre* at 619, citing *Day and Dent* at 108.
[15] Accepted in the context of s 553C also: *Hall v Poolman* (2007) 65 ACSR 123 at [422].
[16] Nor, for that matter, the decision in *Day & Dent*.

on the ratio in that case and lacks a coherent basis to distinguish one beneficial interest from another, for the purpose of applying s 553C.

24. The Full Court's attempt to provide a principled basis for the creation of this distinction is unsound. To do so, the Full Court placed emphasis (at **J**[143]) upon the description of voidable transactions supplied by Barrett JA in ***Fortress Credit*** *Corporation (Australia) II Pty Ltd v Fletcher* (2014) 87 NSWLR 728 at [125]-[129].

25. In *Fortress Credit*, Barrett JA observed (at [128]) that the *"benefit of the recovery inures wholly for the benefit of the persons who will participate under the winding up"*. That statement, and the Full Court's emphasis upon it, must be approached with caution. The view that the proceeds of recovery are held *"wholly for the benefit"* of participating creditors is redolent of the position expressed in English authority[17] that a company in liquidation no longer beneficially owns its property, or that such property becomes *"impressed…with a trust"* by reason of the winding up.[18] That view was rejected by McHugh J in *Commissioner of Taxation v* ***Linter Textiles*** *Australia Ltd (In Liq)* (2005) 220 CLR 592 at 634 [127], in which his Honour concluded that *"Australian authority has favoured the view that beneficial ownership of the assets of a company in liquidation remains with the company"*.[19] More recent authority similarly holds that the proceeds of a recovery action by the liquidator (including unfair preference recoveries) remain the property of the company.[20]

26. Contrary to the conclusion expressed at **J**[151], it is nothing to the point that the company in liquidation is subject to the rights and obligations imposed by the Corporations Act for the purpose of the winding up. A party asserting a claim against another may well have competing calls upon the fruits of its claim, or it may owe obligations to deal with those proceeds in a particular way. It does not follow that the nature of the interest pursued by the claimant is transformed by reason of those ancillary obligations. Moreover, the Full Court's conclusion that the search for beneficial interests is limited to those considered *"relevant"* for this purpose, is difficult to reconcile with the remedial purposes served by statutory set-off provisions

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[17] *Re Oriental Inland Steam Co; ex parte Scinde Railway Co* (1874) LR 9 Ch App 557 at 559, 561; *Inland Revenue Commissioners v Olive Mill Ltd (In Liq)* [1963] 1 WLR 712 at 726-727; *Ayerst v C&K Construction Ltd* [1976] AC 167; *Mitchell v Carter* [1991] 1 BCLC 673 at 686.

[18] *N A Kratzmann Pty Ltd (In Liq) v Tucker (No 2)* (1968) 123 CLR 257 at 300-301, citing *Re Yagerphone Ltd* (1935) 1 Ch 392 at 396.

[19] Citing ***Re Starkey*** [1994] 1 Qd 142. See also to like effect the plurality view expressed at CLR p 612.

[20] *Cook v Italiano Family Fruit Company Pty Ltd* (2010) 190 FCR 474 at [42].

and the necessity to give the reach of statutory set-off provisions (such as s 553C) *"the widest possible scope"*.[21] Once it is accepted that the company remains beneficially interested in the proceeds of the recovery of the claim against the creditor, the mutuality demanded by the text of s 553C is satisfied; both company and creditor assert claims against the other in respect of property of which they remain beneficially entitled, and which ultimately sound in money. That is sufficient.

Ground 2 - The Full Court's Second Core Holding – The Contingency of the Interest

27. The Full Court's second holding against mutuality concerns the asserted lack of any claim (of a vested or contingent nature) by the company against the creditor at the commencement of the winding up (**J**[138]; [154]). This holding similarly reflects the Full Court's narrowing of the availability of set-off in a manner which neither the text of s 553C, nor authority, can support.

28. The relevant principle with respect to the sufficiency of contingent claims was expressed by Dixon J in *Hiley* (extracted at [18] above). As his Honour observed, it is enough that the mutual dealings *"involve"* contingent rights and obligations which afterwards *"in the event that happen…mature or develop into pecuniary demands capable of set off"* (at 497). The correctness of that principle was not doubted by the Full Court below. Nonetheless, the Full Court concluded (at **J**[138]; [154]) that the necessary mutuality could not exist because, at the time of the transaction, there is *"no contingent right or equity, or obligation to have repaid, or to repay, the payment"*. In reaching this conclusion, the Full Court observed (at **J**[138]) that *"one may, depending on the facts, foresee the risk or possibility or likelihood of a winding up"*.

29. Two errors arise from this approach. **First**, the mutuality demanded by s 553C must exist *"at the date of the commencement of the winding up"*,[22] not at the date of the transaction as suggested by the Full Court. It is sufficient that, as at that date, there exist mutual dealings which involve rights or obligations capable of maturation or development into pecuniary demands. It is immaterial for the purpose of this enquiry whether, at the time of the receipt of the payment by the creditor from the company, a winding up was foreseeable by the creditor or the company.[23]

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[21] *Gye v McIntyre* at 619, citing *Day and Dent* at 108.

[22] *Hiley* at 497 (Dixon J).

[23] Except insofar as this foreseeability may impact the application of the exception under s 553C(2), or the defence under s 588FG(2).

30. **Secondly**, it is not correct to say (*c.f.* **J**[138]) that there is no such contingent right or obligation capable of maturation or development into a pecuniary demand as at the date of the commencement of the winding up. The nascent liability of the creditor to disgorge a preference exists at the date of the commencement of the winding up, subject to the liquidator prosecuting a claim for an order under s 588FF to recover that payment. There is no reason within the text of s 553C, nor as a matter of principle, why such a contingency is insufficient to answer the description of Dixon J in *Hiley*. The choice to prosecute a claim, and success in doing so, represent the "*events that happen*" which "*mature or develop*" the contingent liability of the creditor into an actual obligation to repay a preference payment to the company.

31. The possibility of a future claim for the recovery of an unfair preference was correctly held to be a contingent claim by Palmer J in ***Hall v Poolman*** [2007] NSWSC 1330; 65 ACSR 123 at 215-216,[24] which concerned a liquidator's claim for insolvent trading against a company's former directors under s 588M. One of those directors, Mr Irving, asserted a set off against the company under an indemnity deed. Palmer J noted (at 215) that the facts giving rise to a director's liability for an insolvent trading claim existed at the relevant date, *"if the Liquidators prosecuted a claim"*.[25] His Honour referred to the emphasis placed by the High Court in *Gye v McIntyre* upon the *"widest possible scope"* to be afforded to statutory set off provisions.[26] The Full Court below summarily disapproved of the conclusion of Palmer J in *Hall v Poolman*, with the Chief Justice observing simply (at **J**[189]) that he considers *"it to be wrong"*, without further analysis. Such criticism is unfounded; the view of Palmer J was correct.

32. The conclusion of Palmer J in *Hall v Poolman* is also consistent with the earlier decision of ***Vale v TMH*** *Haulage Pty Ltd* (1993) 31 NSWLR 702, which considered whether a claim for insolvent trading under s 556 of the *Companies (New South Wales) Code* was admissible to proof in the subsequent bankruptcy of the company's former director on the basis that it existed as a contingent claim at the relevant time.

33. Priestley JA (with whom Meagher and Sheller JJA agreed) concluded (at 710) that such a claim was relevantly contingent as, upon the satisfaction of the criterion within

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[24] The reasoning of Palmer J in this respect was not disturbed on appeal: *Hall v Poolman* [2009] NSWCA 64; 75 NSWLR 99.

[25] Emphasis added. His Honour also referred (at 216) to the emphasis placed by the High Court in *Gye v McIntyre* upon the *"widest possible scope"* to be afforded to statutory set off provisions.

the section, liability would follow.[27] Priestley JA noted (at 710) that such actions were subject to positive defences but that it was *"realistic to regard the possibility"* of a later claim by the company against the director for insolvent trading as relevantly contingent. In reaching its conclusion below, the Full Court did not directly consider the decision in *Vale v TMH* although cited by the appellant below.

34. Amongst the authorities concerning the nature of the relevant contingency, the decision of Hodgson J in ***Shirlaw*** *v Lewis* (1993) 10 ACSR 288 is particularly compelling. In that case, a business sale agreement was repudiated by the purchaser, which entered liquidation shortly thereafter. The vendor (through receivers) proceeded to take possession of, and sell, the company's stock under the terms of that agreement. The liquidator sought to argue that this disposal of the company's stock amounted to a void disposition under s 468 of the Corporations Law. Hodgson J held that there had been mutual dealings between the parties prior to the winding up in the sense described in *Gye v McIntyre*. His Honour concluded (at 296) that what had *"ultimately happened was the crystallisation of mutual obligations arising from these pre-liquidation dealings"*. It did not matter to this result that the avoidance of the agreement at the suit of the liquidator was made possible only by reason of the statutory mechanism under s 468 and that, by definition under that mechanism, the actual disposition being avoided did not occur until after the after the winding up. *Shirlaw* has been followed on the above point in several cases.[28]

35. The Full Court considered the decision in *Shirlaw* from **J**[191], declining at **J**[212] to express any view as to whether it was correctly decided. Rather, the Full Court sought to distinguish *Shirlaw* on the basis (*inter alia*) that the relevant contractual right discussed by Hodgson J finds no parallel with a preferential payment made to a creditor (**J**[211]). The latter, the Full Court held, did not give rise to a contingent right or equity *"of any kind in the company to require repayment"*. Contrary to that conclusion, there is no principled point of distinction in the reasoning of Hodgson J and the present case. To return to the guidance of Dixon J in *Hiley*, the relevant contingency is satisfied where the parties' mutual dealings *"involve rights or obligations"* which *"mature or*

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[27] Following *Official Trustee in Bankruptcy v CS and GJ Handby Pty Ltd* (1989) 21 FCR 19.

[28] *Facade Treatment Engineering Pty Ltd (in liq) v Brookfield Multiplex Constructions Pty Ltd* [2016] VSCA 247 at [224]; White J in *JLF Bakeries Pty Ltd (In Liquidation) v Baker's Delight Holdings Ltd* [2007] NSWSC 894; 64 ACSR 633 at [41].

develop" into pecuniary demands capable of set off. The company's right to require repayment of the preference is contingent upon the commencement of a winding up and the pursuit by the liquidators of an action under s 588FF. Nothing in s 553C precludes these dual contingencies from constituting the *"events that happen"* to mature or develop the rights and obligations into pecuniary demands. So understood, the Full Court's attempt to distinguish *Shirlaw* fails. The reasoning of Hodgson J is correct and provides forceful support for the appellant's contention in this appeal.

36. One further authority is of note, being the decision of Mansfield J in in ***Re Parker*** (1997) 80 FCR 1, subsequently described by Young JA as *"a thoroughly reasoned judgment based on authority"*.[29] In *Re Parker*, the liquidator sought to recover the sum of $314,796.73 against the parent company of Barossa Ceramics SA Pty Ltd for insolvent trading, pursuant to ss 588V and 588W of the *Corporations Law*.[30] The parent company had submitted a proof of debt for a sum exceeding the liquidator's claim. The liquidator applied for directions under s 511 of the *Corporations Law* as to whether the parent company was entitled to the benefit of a set-off under s 553C. After noting the liberal construction to be afforded to set-off provisions, including in respect of the broad expression in s 553C as to *"other mutual dealings"*,[31] his Honour concluded (at 9-10) that the claims arising from other dealings must exist as contingent as at the decisive date and be of a kind which will ultimately mature into pecuniary demands capable of set-off. His Honour concluded that there was no reason in either logic or principle to exclude from the operation of s 553C a statutory debt for insolvent trading, being a contingent claim arising from *"other dealings"*.[32]

37. Next, his Honour addressed the argument that the claim was not brought by the company but by the liquidator. His Honour held (at 11) that the bringing of the claim by the liquidator and not the company itself was of no consequence in the context of s 553C. His Honour reasoned that the enforceability of a claim by a liquidator is *"but the procedural device for enforcing what is clearly a claim of the company"*. Although not reached by reference to them, his Honour's conclusion in this respect is consonant with the reasoning in *Re Starkey* and *Linter Textiles*. If, as those cases demonstrate,

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[29] ***Buzzle Operations*** *Pty Ltd (In Liq) v Apple Computer Australia Pty Ltd* (2011) 81 NSWLR 47 at [274].

[30] In equivalent terms to the Corporations Act.

[31] By reference to *Gye v McIntyre* at 623.

[32] (1997) 80 FCR 1 at 10, citing *Re Kolb; Ex parte England v Commissioner of Taxation* (1994) 51 FCR 31.

the fruits of the action remain beneficially owned by the company, the mutuality necessary for s 553C cannot be lost simply because those fruits are gathered by the company's agent.[33]

38. The Full Court sought to distinguish *Re Parker* on the basis that ss 588V and 588W served a statutory purpose distinct from that served by s 588FF (**J**[184]). The former, the Full Court observed, protects a subsidiary from a contravention of the Corporations Act by the parent company by providing a statutory action to recover the debts incurred by the subsidiary as a consequence of it trading whilst insolvent. The Court thus concluded that it was unnecessary to consider the correctness of the decision in *Re Parker*.[34] It is to be noted, however, that each of ss 588W and 588FF exist within Part 5.7B of the Corporations Act and provide a means for the recovery of property of the company for the benefit of creditors. In either case, the cause of action is directed at the restoration of the company's pool of assets. That one regime is concerned with the recovery of preferences, and the other with mitigating the effect of insolvent trading, is not a principled point of distinction. The Full Court did not grapple with the correctness of decisions such as *Shirlaw*, *Re Parker* and *Buzzle*,[35] nor has it provided a sound basis upon which one could conclude that the intersection between unfair preferences and set-off raises bespoke questions that do not apply to related recovery provisions. This appeal thus exists in a larger statutory context which, when properly analysed in that manner, confirms the conclusions the appellant seeks.

Ground 3 - Introduction of s 553C of the Corporations Act (The Harmer Report)

39. The introduction of s 553C as part of a package of reforms was the subject to a lengthy and considered scrutiny. Section 553C was introduced by the *Corporate Law Reform Act 1992* (Cth), following the enquiry of Australia's insolvency laws by the Australian Law Reform Commission (**ALRC**) recorded in its 1988 "**Harmer Report**".[36] The Full Court observed (at **J**[101]) that the ALRC's approach to its recommendations for the

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[33] It is well established that a liquidator is an agent of the company: *Thomas Franklin & Sons Ltd v Cameron* (1935) 36 SR (NSW) 286 at 296 (Davidson J).

[34] And by extension, the dicta of Young JA in *Buzzle Operations*. See also: **J**[213]; *Smith v Boné* (2015) 104 ACSR 528 at 589 (Gleeson J); *Stone v Melrose Cranes and Rigging Pty Ltd* (2018) 125 ACSR 406 at 480-481 (Markovic J).

[35] Other authorities note *Re Parker* as controversial but did not decide the matter since it was not fully argued by the parties. See: *Hussain v CSR Building Products Pty Ltd* (2016) 246 FCR 62 at 107 (Edelman J); *Re Force Corp Pty Ltd (in Liq)* (2020) 149 ACSR 451 at 473 (Gleeson J).

[36] Australian Law Reform Commission, *General Insolvency Inquiry*, Report No 45 (1988).

enactment of specific provisions dealing with the avoidance of transactions, was to *"maintain the policy of the existing law"* (Harmer Report, [630]-[631]). That observation proceeds from the Full Court's earlier conclusions as to the *"tolerably clear"* position in Australia regarding the right of set-off (**J**[99]) and the requirement for mutuality in the operation of bankruptcy provisions. The conclusions expressed at **J**[99] are unsound for the reasons explained below, and cast a false shadow upon the recommendations within the Harmer Report.

40. Turning first to the content of the Harmer Report, in formulating its proposals for the introduction of s 553C (including draft legislation), the ALRC identified the danger that it would be *"too easy to create set-offs against an insolvent company as the basis of effectively obtaining a preference"*, thus recommending that *"the situations for excluding a right of set-off should correspond to situations where a transaction may be avoided on the basis that it is preferential"*: Harmer Report, [818]. In other words, the Harmer Report recommended that a statutory set-off be made expressly unavailable in answer to a claim for the recovery of a preference. The ALRC proposed draft legislation to put into effect that recommendation,[37] which, if enacted, may well have precluded creditors such as the appellant from obtaining the benefit of the set-off under s 553C (**J**[106]). Notwithstanding the ALRC's express averment to the risk of a creditor *"effectively obtaining a preference",* the recommendation was not adopted by Parliament when enacting s 553C.

41. Before the Full Court, the appellant argued that this reflected a legislative choice by the Parliament to permit (or at least not to expressly curtail) the application of the set-off under s 553C to circumstances involving the recovery of an unfair preference. The Full Court rejected this submission (at **J**[163]) finding that it *"understate[d] the role of s 553C(2)"* and that there was no attempt in the Harmer Report to broaden *"the notion of genuine mutuality."* That reasoning was in error. It overlooks that the Harmer Report self-evidently accepted there would be sufficient mutuality under s 553C to permit a set-off against a claim for the recovery of a preferential payment by a liquidator. There would otherwise have been no risk of the kind sought to be addressed by the ALRC in its draft legislation.

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[37] Harmer Report, Appendix A, pp 153-154.

42. As to that draft legislation, the ALRC proposed an exclusion within s 553C(2) which would have required a creditor seeking the application of the set-off in respect of a debt arising from a transaction made within the 6 months preceding the commencement of the winding up,[38] to prove that it had *"no reason to suspect"* the insolvency of the company.[39] That is to be contrasted with s 553C as enacted, which excludes the operation of the set-off only in circumstances where the creditor *"had notice"* of the fact that the company was insolvent. Two observations can be made as to this distinction: **First**, the language of *"reason to suspect"* finds parallel within s 588FG(2) of the Corporations Act, which prohibits the Court from making an order under s 588FF prejudicing a right or interest of a person (including the creditor) if it is shown that the person had *"no reasonable grounds for suspecting"* that the company was insolvent: s 588FG(2)(b)(ii). Amending the threshold for the exclusion of the set-off under s 553C to those circumstances in which the creditor had *"reason to suspect"* insolvency (as proposed by the ALRC) would, therefore, have corresponded to the threshold under s 588FG(2). In other words, the proof required to overcome s 588FG(2) would have also precluded the use of set-off under s 553C. **Secondly**, the test for *"notice"* under s 553C(2) as enacted imposes a higher threshold than *"reasonable grounds for suspecting"*.[40] By maintaining this distinction, Parliament chose to leave open the possibility that a creditor might have grounds for reasonably suspecting the insolvency of the company (disqualifying it from the benefit of s 588FG(2)), yet had not *"had notice"* of that company's insolvency (which would trigger the operation of s 553C(2) to exclude the statutory set-off). The ALRC's recommendation Report would have foreclosed this possibility. Nonetheless, the Parliament elected to accept the risk identified by the ALRC as to the possible application of s 553C and the ease of a creditor *"effectively obtaining a preference"*. The Full Court was in error to criticise this result as *"arbitrary"*, or one for which the *"clearest statutory text would be required"* (**J**[156]). The better view is that the consequences of the application of the statutory text is reflective of the legislative will of Parliament, to which opposing policy views must yield.

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[38] The 6-month time period aligns with the voidable transaction provisions including unfair preferences, which requires that the impugned transaction be entered into, or an act be done giving effect to the transaction, within a 6-month period ending on the "relation-back day": Corporations Act, s 588FE(2)(b).

[39] Harmer Report, Appendix A, pp 153-154.

[40] *Jetaway Logistics Pty Ltd v Deputy Commissioner of Taxation* [2009] VSCA 319; 26 VR 657 at 661-662.

The Historic Position: Errors in the "No Change" Proposition

43. In considering the Harmer Report, the Full Court suggested an equivalency (**J**[106]) between s 553C of the Corporations Act and s 86 of the Bankruptcy Act. The Full Court adopted this equivalency to conclude that *"[n]o change was suggested as to the elements or conception of the set-off"*, with the implicit suggestion that the position under s 86 of the Bankruptcy Act was imported into s 553C. That analysis is doubtful for a number of reasons.

44. **First,** it overlooks a fundamental distinction between the personal and corporate insolvency regimes. In the case of personal insolvency, where a debtor becomes a bankrupt, the property of the bankrupt vests *"forthwith"* in the trustee: Bankruptcy Act, s 58(1). That position is to be contrasted with corporate insolvency. The property of a company in liquidation does not vest in its liquidator. The company remains possessed of, and beneficially interested in, its property.[41] Importantly, the company's maintenance of ownership extends to the proceeds of an action to recover an unfair preference.[42]

45. **Secondly**, the *"no change"* analysis of the Full Court carries the implicit assumption that courts have historically disallowed the application of statutory set off in answer to a claim for the recovery of unfair preferences. Before the Full Court, the appellant examined a number of authorities to illustrate why those decisions did not support the sweeping proposition that set-off has been historically disallowed in the case of unfair preferences.[43] Those authorities fall into two classes.

    a. **First**, certain decisions support the view that statutory set-off is available in answer to a claim for the recovery of a preference, where the debt sought to be set off is separate and distinct from the debt the payment of which is avoided as a preference. This appeal concerns this class of case.

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41 *Commissioner of Taxation v Linter Textiles Australia Ltd (In Liq)* (2005) 220 CLR 592 at 612 [54], in which the majority agreed with the proposition: *"Whether the company is insolvent or solvent, the company holds its property beneficially but subject to the statutory scheme of liquidation under which the liquidator is to pay creditors and distribute any surplus among members."*

42 *Cook v Italiano Family Fruit Company Pty Ltd* (2010) 190 FCR 474 at [42].

43 *Re Washington Diamond Mining Co* [1893] 3 Ch 95; *Lister v Hooson* [1908] 1 KB 175; *Re A Debtor* [1927] 1 Ch 410; *Re Clements; ex parte Trustee* (1931) 7 ABC 255; *Re Grezzana; Painter v Charles Whiting & Chambers Ltd* (1932) 4 ABC 203 at 206 (Paine J); *Re Smith; ex parte Trustee, J Bird Pty Ltd v Tully* (1933) 6 ABC 49 at 57 (Lurkin J); *Re Amour* (1956) 18 ABC 69; *Calzaturficio (In Liq) v NSW Leather* [1970] VR 605; *Hamilton v Commonwealth Bank of Australia* (1992) 9 ACSR 90

b. **Secondly**, some of the earlier decisions prohibit the use of set off in circumstances of circularity; where the debt sought to be applied by way of set off is the same as the debt the payment of which is avoided as a preference. This appeal does not concern this second class of case.

46. As to the first class of case, three historic decisions are of particular significance. Contrary to the analysis of the Full Court, each of these cases support the view that courts have not historically prohibited set-off in the context of unfair recovery actions. These decisions repay a careful reading.

47. The decision of Lindley LJ in ***Re Washington*** *Diamond Mining Co* [1893] 3 Ch 95 is of particular significance in this context. In that case, the directors were paid £70 by a company in respect of unpaid directors' fees, having also paid the company £70 for unpaid share capital. In the subsequent winding up, the liquidator sought to recover the £70 payment to the directors as a preference. The question arose as to whether set off was available so as to *"render valid a payment by the company, which but for* [set off] *would be a fraudulent preference"*.[44]

48. The Full Court considered the decision in *Re Washington* at some length (**J**[62]*ff*), placing emphasis (**J**[65]) on the peculiar nature of the action under the 1883 legislation (which presumed the preferential effect upon proof of intention) and sought to distinguish the case on the basis that there had in fact been *"no injury to the estate by the round robin of cheques"* (**J**[75]). This attempt to distinguish the analysis of Lindley LJ is unpersuasive. The question confronting Lindley LJ in *Re Washington* was not answered by an assessment of whether the assets of the company had in fact been diminished and the reasons of his Lordship do not reveal such a process of reasoning. Rather, it is apparent that Lindley LJ would have allowed the claim for set off against the liquidator's claim for a preference had it been an ordinary trading debt, without reference to whether there was an injury to the company's assets. His Lordship disallowed the set off only because of specific provision in the *Companies Act 1862*[45] prohibiting set off against calls for unpaid share capital.[46]

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[44] [1893] 3 Ch 95 at 108, 111 (Lindley LJ).

[45] The parallel to s 553A of the Corporations Act.

[46] The earlier decision of the Court of Appeal in *Re Anglo French Cooperative Society;* ***Ex parte Pelly*** [1882] 2 Ch 492 may be distinguished. *Ex parte Pelly* was not a preference case and turned on the meaning of s 165 of the *Companies Act 1862* which provided for the recovery of funds criminally misappropriated from

49. Similarly, the decision in ***Lister*** *v Hooson* [1908] 1 KB 175 does not support the conclusions expressed at **J**[75]-[76]. It is true that the majority in *Lister*, (Vaughan-Williams and Buckley LLJ) did not refer to the judgment of Lindley LJ in *Re Washington* when declining to permit a set off in bankruptcy against a trustee's claim to avoid a payment made in consideration of marriage. However, the judgment of Fletcher Moulton LJ in *Lister* is of particular significance. Whilst speaking in dissent as to the result, Fletcher Moulton LJ accepted that the decision of Lindley LJ in *Re Washington* established that the *"right to set-off existed in the much stronger case of payments void as fraudulent preferences"*. The Full Court's explanation of the result in *Lister*, and its characterisation of the *"real debate"* (**J**[76]) in that case, does not detract from the holding of Fletcher Moulton LJ as to the significance of the judgment in *Re Washington*. Fletcher Moulton LJ did not identify the foundation of the decision of Lindley LJ in *Re Washington* on the basis advanced by the Full Court.

50. The third decision warranting closer attention is that of the Court of Appeal in ***Re A Debtor*** [1927] 1 Ch 410. Within a bankruptcy, Astbury and Clauson JJ declined to permit a director to apply the set-off with respect to the same debt underlying the payment sought to be recovered as a preference. That is not this case.

51. The Full Court acknowledged that Astbury J in *Re A Debtor* was principally concerned with the second class of case identified in paragraph [45] above (**J**[85]). That may be so, but it does not represent the entirety of what his Honour observed in *Re A Debtor* nor does it reveal the process of reasoning by which that result was reached. Astbury J in fact crystallised the significance of the distinction between the two classes of case, noting that Lindley LJ in *Re Washington* was concerned with the application of a set off in respect of *"two totally separate debts or credits"*. Astbury J accepted that, but for the specific statutory prohibition on the use of set off against a company's call for unpaid share capital, a right of set off in answer to the preference would have been available to the defendants in *Re Washington*.[47] Had the facts in *Re A Debtor* involved – as they do here – separate and distinct debts, the discussion by Astbury J of *Re Washington* compels that set off would have been permitted. To the extent that the Full

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the company. See: Jessel MR (at 503), Brett LJ (at 505, 507) and Cotton LJ (509-510). See also: ***Re Daintree****; ex parte Mante* [1900] 1 QB 546 at 572-573 (Lindley LJ), a case concerning the set off of contingent debts following bankruptcy. The court did not refer to *Ex parte Pelly* or *Re Washington*.

[47] [1927] 1 Ch 410 at 416.

Court's interpretation of the reasons of Astbury J holds otherwise (**J**[86]), it is incorrect.

52. These authorities, and those which follow them, do not admit of the Full Court's conclusion at **J**[99] that the *"tolerably clear accepted position in Australia"* at the time of the enactment of s 553C was to prohibit the application of set-off in the case of unfair preferences. Upon closer analysis, these authorities support the contention that, except in cases of impermissible circularity, the statutory set-off was available. At the very least, the authorities reveal that the position in Australia at the time of the enactment of s 553C was far less certain than confidently stated by the Full Court.

10 **Conclusion: The Proper Construction of s 553C of the Corporations Act**

53. The outcome of the present appeal is dictated by the statutory text. Accordingly, it is to that text that we return in order to make the following concluding observations.

54. **First**, s 588FA(1) defines *"unfair preference"* as a transaction given by the company to the creditor which results in the creditor receiving from the company, in respect of an unsecured debt, more than it would if the transaction were set aside and the creditor were to prove in the winding up. Section 588FE then imposes additional requirements applicable in the ordinary case,[48] including that the transaction be an *"insolvent transaction"* of the company,[49] and that it occur within the 6 months ending on the relation-back day.[50] Each of these *"elements"*,[51] or relevant *"facts"*,[52] or the *"conduct*
20 *constituting the contravention"*[53] under ss 588FA and 588FE are capable of existence as at the relevant date for the purpose of s 553C.

55. **Secondly**, in light of the recognised width of the expression *"mutual dealings"* (extending as it does from correspondence, negotiations, *"communings"* to other relations occurring within a business setting),[54] there is no difficulty in recognising the

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[48] As distinct from a case where the company was under administration, subject to a deed of company arrangement or under a form of restructuring, at the time of the transaction: s 588FE(2A), (2B), (2C) and (2D).

[49] Corporations Act, s 588FE(2)(a)

[50] Corporations Act, s 588FE(2)(b)

[51] To adopt the expression of Dixon J in *Hiley* at 498

[52] To adopt the expression of Palmer J in *Hall v Poolman* at 215.

[53] To adopt the expression of Mansfield J in *Re Parker* at 11.

[54] See *Gye v McIntyre* at 625: *"[dealings] is, none the less, of very wide scope which embraces far more than a legal binding contract or 'deal'. Even if it be correct to construe "dealings" in s 86 as confined to a commercial or business setting, it covers the communings, the negotiations, verbal and by correspondence, and other relations which occur or exist in that setting."*

relationship of the appellant (as vendor) and second respondent (as purchaser) as giving rise to the mutual dealings necessary for the application of s 553C.

56. **Thirdly**, the fact that the maturation or development of the elements for the recovery of an unfair preference requires the liquidator to first advance a claim against the creditor cannot deprive those mutual dealings of their contingent character for the purpose of s 553C, as at the time of the commencement of the winding up.

57. **Fourthly**, it being an agreed fact that the appellant did not have notice of the insolvency of the company at the date it gave its credit to the company (see [6] above), it follows that the critical provision, which is 553C(2) in the form enacted following Harmer (see [42] above), does not disqualify the appellant from the set off.

58. The Full Court therefore fell into error when answering the question referred for its consideration in the negative. The correct view, that the set-off applies to the present circumstances of a separate debt in which the claimant has no notice of the company's insolvency at the time of giving credit maintains fidelity to the language of the statute, is not discordant with principle and is consistent with earlier authority.

PART VII: ORDERS SOUGHT

59. The appellant seeks the following orders: (1) the appeal be allowed; (2) the orders of the Full Court of the Federal Court of Australia made on 16 December 2021 be set aside and in lieu thereof, the answer to the question reserved by Derrington J for consideration of the Full Court of the Federal Court of Australia pursuant to s 25(6) of the *Federal Court of Australia Act 1976* (Cth) be answered "Yes"; and (3) the respondents pay the appellant's costs of this appeal and of the proceedings below.

PART VIII: ESTIMATE OF TIME FOR ORAL ARGUMENT

60. The appellant estimates that it will require 2 hours in chief and 30 minutes in reply.

Dated: 30 June 2022

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IN THE HIGH COURT OF AUSTRALIA
BRISBANE REGISTRY

B19 of 2022

BETWEEN: **METAL MANUFACTURERS PTY LIMITED (ACN 003 762 641)**
Appellant

and

GAVIN MORTON AS LIQUIDATOR OF MJ WOODMAN ELECTRICAL CONTRACTORS PTY LTD (IN LIQUIDATION) (ACN 602 067 863)
First Respondent

MJ WOODMAN ELECTRICAL CONTRACTORS PTY LTD (IN LIQUIDATION) (ACN 602 067 863)
Second Respondent

ANNEXURE TO THE APPELLANT'S SUBMISSIONS

Pursuant to paragraph 3 of the *Practice Direction No 1 of 2019*, the Appellants set out below a list of the constitutional provisions, statues and statutory instruments referred to in these submissions.

No.	Title	Provision(s)	Version
Constitutional Provisions			
1.	*Nil*		
Legislation			
Commonwealth			
2.	*Bankruptcy Act 1966* (Cth)	ss 58, 86	Current (1 June 1966 – present)
3.	*Corporations Act 1989* (Cth) s 82 ('Corporations Law')	ss 468, 511, 588V, 588W	Act no longer in force (14 July 1989 - 15 July 2001)

No.	Title	Provision(s)	Version
4.	*Corporations Act 2001* (Cth)	Pt 5.7B, ss 553A, 553C, 556, 558, 562, 562A, 563, 563AA, 563A, 588FA, 588FI, 588FE, 588FF, 588FG, 588M, 588V, 588W	Historical Versions: 1 July 2018 – 17 September 2018 (Comp No. 88); 18 September 2018 – 21 September 2018 (Comp No. 89); 22 September 2018 - 18 October 2018 (Comp No. 90); and 19 October 2018 – 12 March 2019 (Comp No. 91).
5.	*Corporate Law Reform Act 1992* (Cth)	s 92	Current (24 December 1992 – present)
6.	*Federal Court of Australia Act 1976* (Cth)	s 25	Current (9 December 1976 – present)
7.	*Judiciary Act 1903* (Cth)	s 78B	Current (25 August 1903 – present)
State			
8.	*Companies (New South Wales) Code 1981* (NSW)	s 556	Subordinate instrument no longer in force (30 December 1981 – 1 July 2008)
Other			
9.	*Companies Act 1862* (Imp), 25 & 26 Vict c. 89	ss 164, 165	Historical version (1862 - 1908
Statutory Instruments			
10.	*Nil*		