

CITY INSOLVENCY DISCUSSION GROUP

Wednesday, 2 October 2019

TOPIC

We've got trust issues: Key practice points for winding up insolvent trustee companies

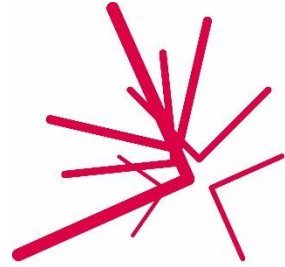
PRESENTED BY

Tom Darbyshire, Partner and Conor Breheny, Senior Associate
Kott Gunning Lawyers



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We've got Trust Issues

CIDG

Presented by Tom Darbyshire, Partner

Conor Breheny, Senior Associate

2 October 2019

Introduction to trusts

- Separates legal and beneficial ownership
- Discretionary trusts for businesses very common
 - tax efficiency
 - asset protection
- Trustee is most often a Pty Ltd
- Liquidation of trustee companies has always created problems of differentiating between trust and company assets
- Recent cases have revealed acute problems with exercising power of sale over trust assets

The problem

- Express trusts are governed by a trust deed; there are many such deeds but they have some common features
- Problematic clauses for insolvency:
 - ipso facto clause; automatic removal of trustee in event of insolvency;
 - clauses empowering guardians to amend deed or replace trustee.
- Removal of insolvent trustee company leaves no-one in charge of trust
- It creates a **bare trust**, where company is legal owner but has no power of sale
- Liquidator **cannot sell company/trust assets** & cannot distribute proceeds to creditors

The solution

- Two ways to resolve the problem:
 - Orders under *Corporations Act* granting liquidator power of sale over trust assets; or
 - Orders appointing liquidator as receiver of trust property
- Both types of orders have been granted in the past, but it is now clear that the Court prefers to appoint a receiver;
 - *Re Gembrook Investments Pty Ltd (in liq)* [2019] FCA 1143
 - *Cremin, in the matter of Brimson Pty Ltd (in liq)* [2019] FCA 1023

Appointment of receiver

- Receiver is appointed by the Court (not under the *Corporations Act*)
- Application can be made to:
 - Federal Court via the *Federal Court Act* (Cth); or
 - Supreme Court via the *Rules of the Supreme Court* (WA)
- Applications to Federal Court more common – lots of recent authority
- Court appointment of receiver removes need to notify ASIC

Receiver's powers

- Court appointed receiver = power derived from the Court
- Seek Court orders for receiver's powers that you need
- General powers:
 - *Corporations Act* s 420 (receiver's powers); or
 - *Corporations Act* s 477(2) (liquidator's powers)
- Specific powers:
 - Power of sale
 - Power to distribute proceeds of sale
 - Power to disclaim trust property

Power limited to trust assets

- When company's only activity is as trustee of one trust, application & distribution reasonably simple
- Trust assets available for distribution to satisfy trust liabilities
- More complex situations
 - company simultaneous trustee of multiple trusts
 - company simultaneously operating in its own right **and** as trustee
- Liquidator must investigate how the company operates
- Trust/company assets must be apportioned to proper creditors as appropriate

Court application: practice points

- Possible orders required:
 - Appointment as receiver: *Federal Court of Australia Act* s 57(1)
 - Powers needed to deal with assets: *Corporations Act* s 420 or 477(2)
 - Orders for distribution of proceeds: *Corporations Act* s 556
 - Deemed approval of transactions completed in breach of trust: *Trustees Act (WA)* s 89 (or retrospective appointment as receiver)
 - Relief from civil liability for breach of trust: *Corporations Act* s 1318(1)
 - Exclusion of certain duties and liabilities of receiver
 - Notification of stakeholders
 - Remuneration/costs as receiver
 - Costs of application

Affidavit in support

The Affidavit in support should address the following issues:

- Circumstances and background to appointment
- Investigations
 - Evidence of company assets being trust assets
 - Evidence that no replacement trustee appointed
- When become aware of trustee status
 - Disclosed in ROCAP (Part B, Question B4)
 - Copy of trust deed
 - Indicators from other records (e.g. tax records, invoices, leases)

Affidavit in support

- For *Trustees Act* deemed approval and *Corporations Act* s 1318 relief for transactions without power, evidence of:
 - Honesty
 - Reasonableness (commercial judgment)
 - Good faith
- If seeking remuneration determination for receivership or liquidation:
 - *Insolvency Practice Schedule (Corporations)* s 60-12 factors relevant;
 - *Sanderson v Sakr [2017] NSWCA 38*
 - Evidence of accrued and expected future remuneration

Future developments

- Industry wide problem
- Status quo is untenable
 - Court intervention potentially required in every liquidation of a corporate trustee
 - Uncommercial
 - Artificial distinction between liquidator and receiver (same person)
- Something will have to change at some point

Solutions?

- Stay on *ipso facto* trustee removal clause?
 - Likely ineffective
 - Use of trust powers by liquidator to sell trust assets for creditors
- Amendment of trust deed prior to appointment
 - Removal/amendment of *ipso facto* trustee removal clause
 - Pre-appointment replacement of trustee
 - Likely contrary to law; “fraud on the power”
 - Tension between creditors v beneficiaries
- Any solution likely requires amendment of *Corporations Act* and state trustee legislation – very difficult
- CIDG: Any ideas?

Final tips

- Read the deed
- Determine status of corporate trustee as soon as possible
 - Ensures no trust property disposed of in breach of trust
 - Ensures good faith can be proven if required
- Even if trustee has not been automatically removed, complex situations may still warrant directions from the Court
- If corporate trustee has been automatically removed, it is **settled** that an application to become receiver is required

Contact us

Tom Darbyshire and Conor Breheny

Phone: +61 8 9321 3755

Mobile: +61 421 314 867

Email: tdarbyshire@kottgunn.com.au;
cbreheny@kottgunn.com.au

kottgunn.com.au

Linkedin Kott Gunning

Twitter @kottgunning

Facebook @kottgunningwa

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Thank you!

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Next CIDG Session

Wednesday, 6 November 2019



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