

## Corporations Law conference August 2016

### Three recent developments in insolvency law

Justice Ashley Black

Supreme Court of New South Wales

#### Introduction

In this paper, I will first consider, at some length, developments in the case law dealing with how a court should fix a liquidator's remuneration. I will then note, briefly, several recent cases dealing with claims in respect of voidable transactions in insolvency and the relatively extensive changes to be made by the *Insolvency Law Reform Act 2016* (Cth), from its expected commencement, partly on 1 March and partly on 1 September 2017.

#### Issues as to liquidator's remuneration

The question of liquidator's remuneration, never far from controversy, has again been addressed in recent case law.<sup>1</sup> I will identify different approaches below. I do not express any preference for one approach over the other, both because this is not the forum to do so, and because it is by no means clear that any single approach will resolve the relevant difficulties.

It is, of course, well-established that a liquidator is entitled to reasonable remuneration for its services and that a liquidator seeking such remuneration bears the onus of establishing that the remuneration claimed is fair and reasonable, having regard to the factors specified in ss 473(10) and 504(2) of the *Corporations Act 2001* (Cth).<sup>2</sup> There are well-recognised issues as to how such remuneration should be calculated. There are reasons why liquidators, and other professionals, would prefer to be paid for their services on the basis of time-based remuneration at standard rates. There are also good reasons why consumers of professional services, and of insolvency services in particular, might be sceptical of that approach, both so far as it is time-based and so far as it seeks to treat standard rates as a given.

Before turning to the case law, it should be noted that the Code of Professional Practice for Insolvency Practitioners issued by the Australian Restructuring Insolvency & Turnaround Association ("ARITA") (3<sup>rd</sup> ed, 2014) includes several principles relevant to the remuneration of insolvency practitioners. Principle 10 provides that a practitioner is entitled to claim remuneration and disbursements in respect of necessary work, properly

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<sup>1</sup> For commentary in respect of judicial review of remuneration generally, see J Dickfos "The Costs and Benefits of Regulating the Market for Corporate Insolvency Practitioner Remuneration" (2016) 25 *International Insolvency Review* 56; S Steele, V Chen and I Ramsay, "An Empirical Study of Australian Judicial Decisions Relating to Insolvency Practitioner Remuneration", forthcoming, 2016.

<sup>2</sup> *Re AAA Financial Intelligence Ltd (in liq) (No 2)* [2014] NSWSC 1270 at [26]; *Re Independent Contractor Services (Aust) Pty Ltd (in liq) (No 2)* [2016] NSWSC 106 at [32].

performed in an administration, and explains those concepts.<sup>3</sup> The Code also seeks to mitigate the risks of time-based costing.<sup>4</sup> Principle 11 in turn deals with disclosure of remuneration and provides that:

“A claim by a Practitioner for Remuneration must provide sufficient, meaningful, open and clear disclosure to the Approving Body so as to allow that body to make an informed decision as to whether the proposed Remuneration is reasonable.”

The Code in turn identifies several possible bases of calculation of remuneration, namely time-based charging; prospective fee approval, subject to a cap to a nominated limit; and a fixed fee or a “percentage of a particular factor”, usually assets disclosed or assets realised. The Code also elaborates on the information to be disclosed by a practitioner and when such disclosure is to be made. Principle 12 in turn provides that a practitioner is only entitled to draw remuneration once it is approved and according to the terms of the approval.

#### *The earlier case law*

The issues with time-based claims for remuneration of insolvency practitioners have long been identified in the case law. In *Mirror Group Newspapers Plc v Maxwell (No 2)* [1998] 1 BCLC 638, Ferris J (at 652) observed that time-based remuneration paid no regard to complexity, exceptional responsibility, the effectiveness of the work done and the value or nature of the property dealt with. His Honour also noted (at 652) that:

“First time spent represents a measure not of the value of the service rendered but the cost of rendering it. Remuneration should be fixed so as to reward value, not so as to indemnify against cost. Secondly, time spent is only one of a number of relevant factors ... The giving of proper weight to these factors is an essential part of the process of assessing the value, as distinct from the cost, of what has been done. Thirdly, it follows from the first two points that, as the task is to assess value rather than cost, the tribunal which fixes remuneration needs to be supplied with full information on all the factors which I have mentioned.”

In *Mirror Group*, Ferris J observed (at 645) that a proposition that an insolvency practitioner had recovered £1.672m in assets, and claimed £744,000 in professional fees and £705,000 in legal fees and disbursements, so as to leave a recovery of £43,428 for creditors was “profoundly shocking”. The fact that cases of no, or minimal, returns to creditors after remuneration and costs continue to occur is one reason why issues of liquidator’s remuneration will remain controversial.

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<sup>3</sup> The Code describes “necessary” work as work that is connected with the insolvency administration and done in furtherance of the exercise of the practitioner’s powers and the performance of his or her duties as required by the legislation, the Code of Conduct and applicable professional standards. The Code explains the concept of “properly performed” as excluding work that is done poorly, improperly or needed to be reworked.

<sup>4</sup> Paragraph 14.6 provides that “[i]n time-based charging, the Practitioner must ensure that the number and qualifications of staff allocated to an Administration is appropriate for the nature of the work being performed so that the Administration is completed in the most efficient and effective manner.” Paragraph 14.7 provides that the practitioner should, in time based charging, “ensure that appropriate hourly rates are set for the Administration.”

The observations of Ferris J in *Mirror Group Newspapers* were quoted, with apparent approval, by Finkelstein J in *Re Stockford Ltd; Korda* (2004) 140 FCR 424; [2004] FCA 1682 and have been echoed in several recent cases to which I will refer below. That decision turned on the question whether administrators' remuneration had been fixed by creditors where they had approved an hourly rate without any cap, so as to authorise payment of that remuneration. Finkelstein J there noted (at [2]) that insolvency practitioners' fees have been examined or subject to critical comment in several reports between 1988 and 2003, and that position has not subsequently changed. His Honour also referred to early case law, including *Re Carton Limited* (1923) 39 TLR 194 which had fixed liquidator's fees as a percentage of the value of assets under the liquidator's control. That methodology has again come into focus in the recent case law.

Finkelstein J also noted (at [26]) that the practice that a liquidator's fee was either a fixed amount or a percentage of assets under the liquidator's control changed in the 1950s and 1960s and remuneration of liquidators began to be fixed on a time basis in complicated liquidations. His Honour referred to the adverse comments which have been made as to remuneration on a time basis in earlier case law, including *Re Carton* above, which have been echoed in several recent cases. His Honour observed (at [38]) that earlier English case law, fixing a liquidator's fees in a specific amount or a percentage of the estate, was "based on the notion of conservation of the estate and economy of administration" and recognised that:

"The other view is simply to allow the market to operate in the normal way: Insolvency practitioners should be entitled to charge their usual hourly rates which, at least to a degree, are likely to be competitive."

His Honour also noted (at [39]) that the "conservation approach" may lead insolvency practitioners to forsake liquidations and administrations if they can earn higher incomes in other fields; while that risk could readily be overstated, and it is presumably unlikely that persons who have devoted substantial efforts to qualifying as insolvency practitioners will abandon their field of expertise en masse, there is room for such a concern in respect of lower value liquidations. His Honour also recognised, by reference to US case law, the difficulties with hourly rates as an incentive to over-servicing, a concern that has again been echoed in recent case law. His Honour observed (at [40]) that:

"It seems to me that some balance must be struck between the two opposing views. The balance must achieve some moderation in fees to protect the fund so that creditors can achieve the largest possible return, but not be so moderate as to discourage competent practitioners from providing their important services."

His Honour also identified several factors relevant to the assessment of remuneration, including the time properly given to attending to the company's affairs, the complexity of the case, any responsibility of an exceptional kind or degree in the particular case, the effectiveness with which the liquidator carried out his duties and the value and nature of the property with which he had to deal. Those factors have since been reflected in the statutory provisions to which I will refer below.

Finkelstein J also expressed the view (at [42]) that it was inevitable that insolvency practitioners would wish to have their fees calculated on a time basis in complex or large administrations and that:

“The Courts have endorsed this approach for so long that it is now impossible to reverse the trend.”

His Honour (at [47]) supported the adoption of a “lodestar” approach, drawn from US case law, which first derives a working figure from time costs, as adjusted by reference to appropriate rates and whether the time is reasonably spent and work is adequately supported by evidence, and then further adjusts that figure to the extent that any particular heads of claim are disallowed or a wider further percentage reduction is imposed. The second stage of that approach plainly opens the possibility of discretionary reductions in time-based remuneration.

The decision in *Korda* influenced amendments to the several provisions dealing with fixing insolvency practitioners’ remuneration in the *Corporations Act 2001* (Cth). Subsection 473(10), which was introduced by the *Corporations Amendment (Insolvency) Act 2007* (Cth), specifies several factors to which a court must have regard in setting the remuneration of a court-appointed liquidator under s 473(3) or reviewing it under s 473(5) or s 473(6). Those factors include whether the remuneration is reasonable, taking into account all or any of specified matters, including the extent to which the work performed or likely to be performed by the liquidator was reasonably necessary; the period during which the work was, or is likely to be, performed; the quality and complexity of the work; whether the liquidator was or is likely to be required to deal with extraordinary issues, or accept a higher level of risk or responsibility than is usually the case; the value and nature of any property dealt with, or likely to be dealt with, by the liquidator; whether the liquidator was, or is likely to be, required to deal with other insolvency practitioners; the number, attributes and behaviour, or the likely number, attributes and behaviour, of the company’s creditors; and, if the remuneration is ascertained, in whole or in part, on a time basis, the time properly taken, or likely to be properly taken, by the liquidator in performing the work; and whether the total remuneration payable to the liquidator is capped. These factors correspond to those specified in s 425(8) in respect of receivers, s 449E(4) in respect of administrators and s 504(2) in respect of liquidators in voluntary winding ups.

There are indications of liquidators’ preference for time-based remuneration, and courts’ scepticism of it, in the subsequent case law. In *Conlan v Adams* (2008) 65 ACSR 521; [2008] WASCA 61, McLure JA (as her Honour then was) referred to the earlier decision in *Venetian Nominees Pty Ltd v Conlan* (1998) 20 WAR 96 and summarised the principles that emerged from it as follows (at [28]):

“A liquidator is entitled to remuneration that is fair and reasonable and the liquidator carries the onus of establishing that entitlement. The court also said that in determining the remuneration to which a liquidator is entitled:

— a summary procedure is involved, not unlike that applicable to the taxation of solicitors’ costs, which is not necessarily subject to all the rules that would apply in an action;

— it is the function of the court to determine the remuneration by considering the material proffered and bringing an independent mind to bear on the relevant issues, the initial task being to consider whether, prima facie, the liquidator has made out a case for the determination of the amounts claimed. The court must make an independent assessment even in the absence of objectors, appropriately detailed objections or arguable objections...”

McLure JA also there noted (at [39]) the disadvantages associated with a time-based approach, which the parties had adopted, and also emphasised (at [47]) the importance of proportionality. Those observations were cited with apparent approval, by Brereton J in *Re AAA Financial Intelligence Ltd (in liq) (No 2)* [2014] NSWSC 1270, to which I will refer below.

### *Recent cases adopting time-based costing and issues as to proportionality*

Several recent decisions in both the State Supreme Courts and in the Federal Court of Australia have applied time costing as at least the starting point for a calculation of remuneration, although those decisions also emphasise the need for proportionality between the cost of the work done and the value of the services provided.<sup>5</sup>

In *Thackray v Gunns Plantations Ltd* (2011) 85 ACSR 144; [2011] VSC 380, Davies J observed (at [63]) that the reasonableness of remuneration may be established by evidence of an appropriate benchmark for comparable work by persons with the relevant skills and qualifications and justification of the time spent, and could be adjusted up and down to reflect other factors including unusual complexity of the work or the novelty and difficulties of the issues and the ultimate outcome obtained by the insolvency practitioner. Her Honour also noted (at [64]) that:

“Excessive charging may be indicated if there is a lack of proportionality between the cost of the work done relative to the value of the services provided. But there is no universal approach applicable in all circumstances by which the “reasonableness” of remuneration claimed or expenses incurred should be measured. The size, importance and complexity of the tasks performed are all factors to be taken into account. What is needed is sufficient information for the Court and any objector to have a clear view about what was done so that an assessment can be made about the reasonableness of the claim.” [Citations omitted.]

In *Warner, Re GTL Tradeup Pty Ltd (in liq)* (2015) 104 ACSR 633; [2015] FCA 323, Farrell J also noted (at [70]) community concern as to cases where there was little return to creditors after a liquidator’s remuneration, but also recognised that liquidators may be unlikely to take on work which would bring about positive results for creditors without reasonable remuneration. Her Honour noted (at [71]) that whether remuneration was

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<sup>5</sup> *Thackray v Gunns Plantations Ltd* (2011) 85 ACSR 144; [2011] VSC 380; *Hayes, Re Henry Walker Eltin Group Ltd (in liq) (No 4)* [2015] FCA 656; *Re Traditional Values Management Ltd (in liq) (No 2)* [2015] VSC 126; *Re Traditional Values Management Ltd (in liq) (special purpose liquidator appointed)* [2015] VSC 338; *Re Eastwood Insulation Pty Ltd (in liq)*; *Macks & Anor v Maka & Anor* [2015] SASC 200; *Re Koori Employment Enterprises Co-Operative Ltd (in liq)* [2016] VSC 245; *Smith; In the matter of Oceanic Asset Management Pty Ltd* [2016] FCA 644.

reasonable was not to be assessed solely by time costing or as a percentage of return, and that the value of the work would have to be assessed not only by the return to creditors but also by whether it was necessary to be done, even if it did not generate a return to creditors. Her Honour also referred, with apparent approval, to the factors relevant to the assessment of “reasonable remuneration” identified by Brereton J in *Re AAA Financial Intelligence* above; see also *ACN 104 635 369 Pty Ltd (in liq) (formerly Total Plant Services Pty Ltd) v Hamilton* [2015] FCA 1219 (Gleeson J).

The question of proportionality was also emphasised by the Full Court of the Federal Court in dealing with the remuneration of a court-appointed receiver in *Templeton v Australian Securities and Investments Commission* (2015) 108 ACSR 545; [2015] FCAFC 137. The Court (Besanko, Middleton and Beach JJ) rejected (at [26]) a contention that whether the receiver’s remuneration was reasonable could be determined solely by whether the time spent was reasonable and the application of fixed rates to that time. The Court observed (at [26]–[35]) that the question of proportionality, involving a comparison of the claim to remuneration with the property or activity that was the subject of the insolvency administration or the benefit or gain to be obtained, was an important consideration in determining the overall reasonableness of remuneration. The Court observed (at [30]) that:

“The question of proportionality is an anterior question to consider in order to determine whether time was reasonably spent. If the relevant work plan underpinning the actual time spent and the allocation of personnel at the requisite level of seniority was disproportionate to the nature, importance and complexity of the task and the benefit to be achieved from the task, then it might be said that time spent on the task was not time *reasonably spent*.”

The Court also noted (at [34]) that a lack of proportionality between the cost of the work done and the value of the services provided may support a conclusion of overcharging or excessive remuneration. The Court recognised (at [60]) that a court could appropriately apply a discount to a claim, after making findings as to whether work was necessary and appropriate to be done, and whether it had been done by an appropriate level of staff and efficiently, although their Honours allowed an appeal against the discount that had been applied in that case.

#### *Relevance of percentage of realisations*

Several decisions of Brereton J in the Supreme Court of New South Wales have emphasised the significance of the percentage that a liquidator’s remuneration bears to the level of asset realisations achieved. In *Re AAA Financial Intelligence* above, Brereton J noted the observations of Finkelstein J in *Re Stockford* above but also expressed a greater degree of scepticism as to the ability of market forces to control liquidator’s charges, and noted (at [41]) that “creditors are rarely in a position robustly to negotiate a liquidator’s remuneration” and that “comparative cost is rarely a factor in selection of a liquidator”. Academic commentary has also noted that diverse interests of creditors may

adversely affect their ability to organise, cooperate or effectively review the practitioner's remuneration.<sup>6</sup>

Brereton J observed (at [45]) that:

“In my view, reasonable remuneration cannot be assessed solely by the application of the liquidator's quoted standard hourly rates to the time reasonably spent.”

His Honour noted (at [45]) that the application of standard hourly rates would not reflect several of the factors specified in s 504(2) of the *Corporations Act*, particularly the quality of work performed, the degree of risk and responsibility and the value and nature of the property involved. His Honour also identified a wider criticism of time costing, that it:

“does not reward liquidators for value, but indemnifies them against costs. It disregards considerations of proportionality. ... This must mean that it is wrong to assess 'reasonable remuneration' by reference only to time reasonably spent at standard rates. ... [W]hile time reasonably spent at standard hourly rates is a relevant consideration, it is only one of several, should not be regarded as the default position or dominant factor, and is to be considered in the context of other factors, including the risk assumed, the value generated, and proportionality.”

His Honour's reference to the need to consider those other factors reflects the statutory requirements of ss 473 and 504 of the *Corporations Act*, and there can be little room for controversy as to the relevance of those factors, although views may differ as to how they are to be addressed. His Honour recognised (at [47]) that ad valorem remuneration, based on a percentage of realisations, also had shortcomings, but observed that it was proportionate and incentivised the creation of value.

In that case, the liquidator had already received \$95,000 in remuneration for work done in a prior administration (at [33]) and had funds in hand of \$104,000 at the time of his appointment as liquidator. He realised a further \$76,000 in the course of the liquidation and initially claimed remuneration of \$49,915 for his work as liquidator. Brereton J allowed remuneration of \$36,000, or about 20% of total realisations. In arriving at that amount, Brereton J took into account that debt collection had been outsourced by the liquidator, so as to reduce the risk and responsibility borne by the liquidator, and that a claim for remuneration that amounted to 70% of the amount remaining after costs and disbursements would not be proportionate. His Honour noted that, absent that reduction, the liquidator's claim for remuneration and expenses would have exhausted the trust funds and the only beneficiary of the liquidation would have been the liquidator. That is, of course, the concern that was also identified by Ferris J in *Mirror Group Newspapers* above.

Brereton J has taken a similar approach in several subsequent cases, including *Re Hellion Protection Pty Ltd (in liq)* [2014] NSWSC 1299<sup>7</sup> and *Re Gramarkerr Pty Ltd (No 2)* [2014] NSWSC 1405.<sup>8</sup>

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<sup>6</sup> J Dickfos, “The Costs and Benefits of Regulating the Market for Corporate Insolvency Practitioner Remuneration” above, p 65.

In *Re Independent Contractor Services (Aust) Pty Ltd (in liq) (No 2)* [2016] NSWSC 106 (which is also significant for its treatment of a liquidator's powers in respect of trust assets, and will be addressed by Peter Leech in that respect), Brereton J again expressed the view that liquidators should not necessarily be allowed remuneration at their firm's standard hourly rates for time spent and observed (at [32]) that "[p]articularly in smaller liquidations, questions of proportionality, value and risk loom large" and that "liquidators cannot expect to be rewarded for the time spent at the same hourly rate as might be justifiable where more property is available". In that case, the liquidator's realisations were \$211,799; the liquidator claimed remuneration of \$49,510, which was significantly reduced from that calculated on a time costing basis, with a large part of that claim being applicable to an application for directions that had been made to the Court. Brereton J accepted that the liquidator was entitled to remuneration for activities relating to the resolution of the relevant issues, although his Honour also noted that the risk of that issue had been (at least to some extent) shifted to legal practitioners, and also recognised (at [47]) the importance of not discouraging liquidators from conducting small but difficult liquidations. His Honour allowed remuneration of \$30,000 or about 14% of gross realisations.

His Honour adopted a similar approach in *Re Sakr Nominees Pty Ltd* [2016] NSWSC 709, in dealing with a liquidator's claim for remuneration<sup>9</sup> and for leave to distribute a surplus to contributories under s 488 of the *Corporations Act*. Brereton J referred to his judgment in *Re AAA Financial Intelligence Ltd (in liq) (No 2)* above and (at [16]) reiterated the view that ad valorem remuneration is inherently proportionate and incentivises the creation of value rather than the disproportionate expenditure of time. His Honour also noted (at [22]) that, where an ad valorem approach is adopted, then:

"Normally, the larger the liquidation, the lower the rate of commission will be: rates of commission will decline, as the amount of assets increase, on a sliding scale."

His Honour noted that an allowance of commission at the rates in *Grammarkerr*, of 10% on the first \$100,000 and 5% on the balance, would be generous in those circumstances, although he allowed additional remuneration for additional work that had been required by issues as to the identity of contributories. An appeal has been brought from the decision in *Sakr Nominees*.

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<sup>7</sup> In that case, the liquidator's realisations were \$45,000 although an amount in GEERS funding of \$250,000 was also received; the liquidator sought remuneration of \$47,399, increased from the remuneration that had previously been approved at a creditors' meeting on a time costing basis up to a maximum of \$25,000. Brereton J indicated that he would have approved a lesser amount than approved by the creditors, on a basis of 10% of the first \$50,000 of recoveries, equating to the statutory starting point of \$5,000, and 5% on GEERS realisations although they are not strictly recoveries in the liquidation.

<sup>8</sup> In that case, the liquidator's realisations were \$495,000; the liquidator had initially claimed remuneration of \$64,000 on a time basis but had reduced that claim to approximately \$24,196. Brereton J approached remuneration by reference to a proportion of the funds realised, noting that he would have been inclined to allow an amount of \$27,750, being 10% of the first \$100,000 and 5% on the balance, which was a slightly higher amount than the liquidator's revised claim.

<sup>9</sup> The liquidator had there already drawn down remuneration of approximately \$197,000, which had previously been approved by creditors, and sought further remuneration of \$63,577, which could not be approved by creditors who had been paid out in full.



The relationship between a time-based approach and an approach that has regard to percentage of realisations was recently considered by Robb J in *Clout in his capacity as Liquidator of Mainz Developments Pty Ltd (in liquidation)* [2016] NSWSC 1146, where his Honour noted (at [134]) that, in the several cases that have had regard to percentage-based remunerations, liquidators had generally formulated opening claims for a particular amount, based upon time expended and a scale of fees: for example, *Re AAA Financial Intelligence Ltd (in liq) (No 2)* above at [43]; *Re Gramarkerr Pty Ltd (No 2)* above at [10]; *Re Sakr Nominees Pty Ltd* above at [11]; *Independent Contractor Services Pty Ltd* above at [37]. His Honour went on to observe (at [134]-[135]) that:

“That [ie the claim on a time-based basis] provided a rational and objective starting point for the liquidator’s claim for remuneration, which could be assessed in the context of the other factors made relevant by ss 473(10) or 504(2) of the Act. Thereafter, the court considered in each case specific factors relevant to the work undertaken by the liquidator. Then, having regard to the assets realised and distributed by the liquidator, the court called in aid percentages that appeared reasonable in the particular case to assist the court in judging how to achieve proportionality between the liquidator’s remuneration and the value to creditors of the work done.

The process in which the court engages does not involve the direct adoption of any particular proportion or percentage, but, in a process that involves an evaluative assessment of a number of discretionary factors, the court in an appropriate case – more likely where the value of the assets realised is low, or where the remuneration claimed is a substantial proportion or exceeds the value of the assets realised – the court will adopt an appropriate percentage having regard to the court’s experience of other cases as a guide to assessing the appropriate remuneration for the liquidator in the particular case.”

This approach invites reference to percentage of realisations at least as a test of, and potentially as an alternative to, remuneration claims brought by a liquidator on a time-based basis. Robb J also helpfully referred to several of the cases that have considered time-based claims for remuneration (at [158]ff) and emphasised what may be seen as the overriding consideration, as identified by Barrett J in *Re Anderson Group Pty Ltd; Mann v Anderson* [2002] NSWSC 764 at [12] that:

“In the ordinary course, the process of determination comes down essentially to ensuring that the work upon which the claim was based was work undertaken in the due course of administration and that the amount claimed for having done that work is a fair and reasonable reward for it.”

Robb J noted that a similar observation was made by Brereton J in *Re AAA Financial Intelligence Ltd (in liq) (No 2)* above at [26], and I understand Robb J’s decision in *Mainz Developments* to have approved that approach.

There may be a perception among liquidators and possibly their advisers that remuneration allowed by reference to, or tested by reference to a percentage of realisations will necessarily be less than remuneration allowed on a time-costing basis. That perception may not be well-founded, since remuneration allowed on a time-costing basis can, as the case law indicates, be reduced to achieve proportionality in an appropriate case.

### *The international experience*

The concerns as to remuneration of insolvency practitioners are by no means unique to Australia.

Issues as to the remuneration of insolvency practitioners were considered in the United Kingdom by a report by the Office of Fair Trading (2010) and a further report by Professor Kempson to the Insolvency Service in 2013, which recognised difficulties in creditors exercising control over such remuneration. The *Insolvency (Amendment) Rules 2015* (UK), introduced in the United Kingdom with effect from 1 October 2015<sup>10</sup>, requires insolvency practitioners to provide fee estimates to creditors, giving details of their likely remunerations and expenses, before the basis of their remuneration is determined and, in effect, cap remuneration (but not expenses) at the level of the estimate unless further approval is obtained. That approach broadly corresponds to prospective approval for remuneration, subject to a cap, under Part 15 of the ARITA Code of Professional Practice. There are, of course, obvious challenges in estimating remuneration claims in a complex administration at an early stage. Those rules also require progress reporting as to remuneration and expenses incurred.

In a recent Singaporean decision, *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, Steven Chong J also pointed to similar issues arising in Singaporean insolvency administrations, referring at some length to the decision in *Mirror Group Newspapers* above, and noting the approach to this issue in, inter alia, English and Australian law. His Honour expressed the view (at [52]) that the courts may not have any choice other than to use time-based costs as a starting point for their assessment, but recognised the difficulties with that approach; and also recognised the difficulties with discretionary reductions to the amount of remuneration claimed, although he ultimately imposed such a reduction in that case. His Honour advanced a proposal for costs scheduling, consistent with an approach adopted in the United Kingdom, which would require an insolvency practitioner to pre-estimate its remuneration, and would not permit the insolvency practitioner to exceed that remuneration without further approval.

### *The implications of the recent Australian case law*

Let me now seek to identify several implications of the recent Australian case law:

- First, these issues have always been, and will continue to be, issues of difficulty.
- Second, courts' concerns as to reliance on hourly rates are a continuing theme in the case law and far from a recent development. That concern is shared in the wider community.
- Third, a standard hourly rate that is applied to both large and small insolvencies has the inherent difficulty that large and small insolvencies are arguably different in

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<sup>10</sup> For commentary, see D Milman, "Corporate insolvency in 2015: the ever-changing legal landscape" *Co L.N.* 2015, 368, 1-5; S Morgan, "Insolvency office holder remuneration: the practical aspects of fee approval, challenges and independent reviews" (2016) 29(6) *Insolv Int* 87-92.

character, and creditors face real risks, including of nil returns, from the application of undiscounted standard hourly rates in smaller insolvencies. In a competitive market, hourly rates would be (and in the case of legal practitioners, are) negotiated, including by reference to the size of the relevant transaction.

- Fourth, the recent case law also suggests that a claim for remuneration based on hourly rates is likely to be, at least, tested by reference to a percentage of realisations and possibly, as an appropriate case, displaced by remuneration on that basis or by a mixed approach. The result will not necessarily lead to different outcomes, in quantum, from a court applying a discretionary discount to hourly rates by reference to the factors specified in ss 473(10) and 504(2) of the *Corporations Act*.
- Fifth, the utility of scrutiny of remuneration is reduced, to some extent, by the fact that the Court does not normally approve a liquidator's costs and disbursements.<sup>11</sup> However, the payment of substantial disbursements to other professionals may be indicative of a shifting of, or sharing of responsibility to or with them, which may support a reduction in the remuneration allowed to an insolvency practitioner.
- Sixth, whichever approach is adopted, there will be cases where the complexity of the issues in an insolvency, or the scarcity of assets, are such that the insolvency practitioner's remuneration for work that is reasonably necessary to address those issues, if charged at his or her ordinary rates, and costs and disbursements, would exhaust or substantially dissipate the assets of the insolvent estate, extinguishing or significantly reducing any return to creditors. That difficulty cannot always be resolved by a suggestion that the insolvency practitioner should not undertake that work, because that work may be required by statutory requirements, or because assets may not be recoverable, or a distribution to creditors may not be possible on any reasonable basis, without undertaking that work. There is a policy question whether an insolvency practitioner can fairly expect to charge its usual hourly rates, even for work that is reasonably done and proportionate, in such a case. It is by no means obvious that, in a competitive market, creditors would have contracted to pay such ordinary rates whatever the outcome of the insolvency.
- Seventh, courts continue to recognise that fairness, and necessity, require that insolvency practitioners are reasonably remunerated for their work, however the quantum of that remuneration is determined. Absent a position where insolvency practitioners are bound to accept appointment in smaller or more complex insolvencies, then parties would potentially have difficulty in obtaining their consents to such appointments, and courts would have consequential difficulty in making such appointments, if those appointments were generally unprofitable for insolvency practitioners and their firms.

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<sup>11</sup> For an example of a partly successful challenge to costs and disbursements made out by a deed administrator, see *Re Joe & Joe Developments Pty Ltd (subject to a deed of company arrangement)* [2014] NSWSC 1444.

The *Insolvency Law Reform Act* 2016 (Cth) will also make modest amendments to the process for remuneration of insolvency practitioners from its commencement, expected to be 1 September 2017 for these changes. An external administrator<sup>12</sup> will be able to claim remuneration specified in a “remuneration determination” or, where it is the first practitioner appointed, a minimum fee of \$5000 (exclusive of GST) indexed to the consumer price index. The creditors, a committee of inspection or the court will be able to make a remuneration determination and the court will have power to review such a determination.<sup>13</sup> A cap will be required for remuneration that is determined on a time costing basis.<sup>14</sup> Insolvency practitioners will be prevented, subject to specified exceptions, from directly or indirectly deriving a profit or advantage from the external administration<sup>15</sup> of a company, including from a transaction, sale or purchase for or on account of the company, deriving a profit or advantage from a creditor or member, or a related entity deriving a profit or advantage from the external administration of the company.<sup>16</sup> That provision should prevent remuneration claims being channeled to related entities and then treated as disbursements.<sup>17</sup> There will be provision for appointment of a registered liquidator to review another insolvency practitioner’s remuneration and costs or expenses, by resolution of the creditors and, subject to limitations, by one or more creditor(s).<sup>18</sup> I will briefly refer to other amendments made by the *Insolvency Law Reform Act* below.

### **Claims in respect of voidable transactions under s 588FF of the Corporations Act**

Section 588FF of the *Corporations Act* specifies the orders that a court may make if a transaction is voidable under s 588FE of the *Corporations Act*, as an insolvent transaction including an unfair preference (within the scope of s 588FA), an uncommercial transaction of the company (within the scope of s 588FB), an unfair loan to the company (within the scope of s 588FD) or an unreasonable director-related transaction (within the meaning of s 588FDA). An application under this section may be made during the period beginning on the relation-back day (as defined in s 9) and ending on the later of 3 years after the relation-back day or 12 months after the first appointment of a liquidator in relation to the winding up of the company (s 588FF(3)(a)) or within such longer period as the court orders on an application by the liquidator brought within that period (s 588FF(3)(b)).<sup>19</sup>

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<sup>12</sup> Div 5, s 5-20 of the Insolvency Practice Schedule (Corporations) provides that an external administrator is an administrator of a company, the administrator of a deed of company arrangement in respect of the company or the liquidator or provisional liquidator of the company.

<sup>13</sup> Insolvency Practice Schedule (Corporations) Div 60 Subdiv B.

<sup>14</sup> Insolvency Practice Schedule (Corporations) Div 60, s 60-10.

<sup>15</sup> Insolvency Practice Schedule (Corporations) Div 5, s 5-15 provides that a company is under external administration if it is under administration or a deed of company arrangement has been entered into or a liquidator or provisional liquidator appointed in respect of the company.

<sup>16</sup> Insolvency Practice Schedule (Corporations) Div 60 Subdiv E.

<sup>17</sup> J Dickfos, “The Regulation of Corporate insolvency practitioners: 25 Years on from the Harmer Report (or Everything Old is New Again) (2014) 2 *NIBLeJ* 3 at 40.

<sup>18</sup> Insolvency Practice Schedule (Corporations) Div 90, s 90-24.

<sup>19</sup> *BP Australia Ltd v Brown* [2003] NSWCA 216; (2003) 58 NSWLR 322; 46 ACSR 677; *Tolcher v Capital Finance Australia Ltd* [2005] FCA 108; (2005) 143 FCR 300; 52 ACSR 328; *Australian Securities and*

The power to make “shelf orders” which extend the time for a liquidator to bring proceedings in relation to voidable transactions that are not identified at the relevant time, has been recognised at least since *BP Australia Ltd v Brown* (2003) 58 NSWLR 322; (2003) 46 ACSR 677; [2003] NSWCA 216 and was reconfirmed on appeal in *Fortress Credit Corporation (Australia) II Pty Ltd v Fletcher* (2015) 254 CLR 489; (2015) 89 ALJR 425; [2015] HCA 10.

The interaction between s 588FF and the Court’s procedural rules, including for extensions of time, was considered by the High Court of Australia in *Grant Samuel Corporate Finance Pty Ltd v Fletcher* (2015) 254 CLR 477; (2015) 89 ALJR 401; [2015] HCA 8. The High Court emphasised that the commencement of preference proceedings within the time limit under s 588FF(3), as extended under s 588FF(3)(b) was a precondition to the Court’s jurisdiction under s 588FF; and held that s 588FF “otherwise provided” for the purposes of s 79 of the *Judiciary Act* 1903 (Cth), so that an extension of time under that section could not be supplemented or varied by procedural rules of the Court in which the application has been brought.

In a third decision, in *Fletcher v Anderson* (2014) 292 FLR 269; (2014) 103 ACSR 236; [2014] NSWCA 450, the Court of Appeal considered the position in respect of preference claims against the Commissioner of Taxation under s 588FA of the *Corporations Act* and consequential claims to indemnity under s 588FGA of the *Corporations Act*. The Court of Appeal observed that s 588FGA(2) of the *Corporations Act* creates a statutory liability on the part of the director, in respect of the claim against the Commissioner of Taxation, whether or not the Commissioner ultimately brings proceedings to enforce that statutory liability, and also held that directors were immediately affected by the extension order made under s 588FF of the *Corporations Act* and should have been given notice of the application and an opportunity to be heard. However, the result was not that the extension order should necessarily be set aside, but instead that they should be allowed a further opportunity to be heard as to the question whether that order should have been made.

In *Re Cardinal Group Pty Ltd (in liq)* (2015) 110 ACSR 175; [2015] NSWSC 1761, I granted leave to liquidators to amend a statement of claim to extend their preference claim, where the particular dealings which were the subject of that claim were outside the three year period specified in s 588FF(3) of the Act. I followed the earlier decision of the Full Court of the Federal Court of Australia in *Rodgers v Federal Commissioner of Taxation* (1998) 88 FCR 61; 29 ACSR 270, where the Full Court had held that amendment to an existing proceeding, commenced within time, could add separate transactions based on substantially the same facts. I distinguished the decision in *Fortress Credit Corporation* above on the basis that it concerned the commencement of new proceedings and also noted that, in the particular case, the claim could have been pleaded as a single transaction and the particular dealings that were introduced in the claim could have been added by way of further particulars of that transaction. An appeal

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*Investments Commission v Karl Suleman Enterprises Pty Ltd (in liq)* [2004] NSWSC 1244; (2004) 52 ACSR 103.

from that decision has now been heard by a five-member Court of Appeal and judgment is reserved.

### **Insolvency Law Reform Act**

I should also mention the passage of the *Insolvency Law Reform Act* 2016. The amendments will amend both the *Bankruptcy Act* 1966 (Cth) and the *Corporations Act* to introduce common rules in relation to the registration, regulation, discipline and the registration of corporate and personal insolvency practitioners. The Explanatory Memorandum to the Exposure Draft identifies the purpose of the proposed amendments as including removing unnecessary costs and increasing efficiency in insolvency administrations, aligning and modernising the registration and disciplinary frameworks that apply to registered liquidators and registered trustees in bankruptcy and rules relating to personal bankruptcies and corporate external administrations; promoting market competition on price and quality and “improv[ing] overall confidence in the professionalism and competence of insolvency practitioners”.<sup>20</sup>

The *Insolvency Law Reform Act* will repeal a number of sections that are commonly relied on in applications in the Corporations List, including s 479 (exercise and control of a court-appointed liquidator’s powers), ss 502–505 (appointment and removal of a liquidator in a voluntary winding up, review of a liquidator’s remuneration), s 511 (applications to the Court to have questions determined or powers exercised in a voluntary winding up), s 536 (supervision of liquidators) and ss 600A–600E (Court’s powers in respect of resolutions passed at creditors’ meetings). There are complex transitional provisions.

Some broadly corresponding powers will be introduced in the Insolvency Practice Schedule (Corporations) contained in proposed Schedule 2 of the *Corporations Act*. It is expected that Parts 1 and 2 of the Insolvency Practice Schedule (Corporations) (dealing with registration and discipline of liquidators) will commence on 1 March 2017 and Part 3 (dealing with general rules for the conduct of external administrations) will commence on 1 September 2017. Division 45 of the Insolvency Practice Schedule (Corporations) allows the Court specified powers in relation to registered liquidators, including on its own initiative in Court proceedings or on application by the liquidator or ASIC. Division 70 Subdiv G allows the Court (and also ASIC) a new power to direct an insolvency practitioner to provide information, including information requested by creditors. The Court retains the power to inquire into an external administration under Div 90 Subdivs B and C. In particular, s 90–15 allows the Court to make such orders as it thinks fit in relation to the external administration of a company. Section 90–15(3) gives examples of such orders, which include orders determining any question arising in the external administration of the company; that a person cease to be the external administrator of the company or that another registered liquidator be appointed as the external administrator of the company; in relation to the costs of an action (including court action) taken by the external administrator of the company or another person in relation to the external administration of the company; in relation to any loss that the company has sustained

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<sup>20</sup> Explanatory Memorandum to the Exposure Draft of the Insolvency Law Reform Bill 2014, p 3.

because of a breach of duty by the external administrator; and in relation to remuneration, including an order requiring a person to repay to a company, or the creditors of a company, remuneration paid to the person as external administrator of the company. The Court can exercise that power on its own initiative, during proceedings before the Court; or on application by specified persons under s 90–20.

Div 100, s 100-5 will allow an external administrator to assign any right to sue conferred on him or her by the *Corporations Act*, but court approval for that assignment is required after any action brought by the external administrator has begun. That section seems to preserve the present position, at least in New South Wales, that several statutory claims for compensation arising under the *Act*, which are not rights of action conferred on the liquidator, are not assignable.<sup>21</sup>

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<sup>21</sup> *Boston Commercial Services Pty Ltd v GE Capital Finance Australasia Pty Ltd* (2006) 236 ALR 720; at [51]–[52]; [2006] FCA 1352; *Tosich v Tasman Investment Management Ltd* (2008) 250 ALR 274; [2008] FCA 377 at [37]; *Mijac Investments Pty Ltd v Graham (No 2)* (2009) 72 ACSR 684; [2009] FCA 773 at [31]; *Re Cant (in his capacity as liquidator of Novaline Pty Ltd (ACN 006 622 933) (in liq))* (2011) 282 ALR 49; 85 ACSR 31; [2011] FCA 898 at [19]; *Owners of Strata Plan 5290 v CGS & Co Pty Ltd* [2011] NSWCA 168 at [70]–[72] (holding that s 477(2)(c), as it now stands, does not make assignable causes of action that are otherwise not assignable); *Re Colorado Products Pty Ltd (in prov liq)* (2014) 101 ACSR 233; [2014] NSWSC 789 at [392]–[396]; *Aquatic Air Pty Limited v Siewert* [2015] NSWSC 928 at [87].