IN THE SUPREME COURT OF NEW ZEALAND

SC 39/2005

IN THE MATTER	of a Civil Appeal	
BETWEEN	**TRANSOTWAY LIMITED**	
	Appellant	
AND	**IAIN BRUCE SHEPHARD AND CHRISTINE MARGARET DUNPHY**	
	Respondents	

Hearing 11 November 2005

Coram Elias CJ
Blanchard J
Tipping J
McGrath J
Eichelbaum J

Counsel P D McKenzie QC and D M Law for Appellant
H L Thompson for Respondents

CIVIL APPEAL

10.00 am

Elias CJ Yes Mr McKenzie

McKenzie May it please the Court I appear with my friend Ms Deborah Law for the appellant.

Elias CJ Yes thank you Mr McKenzie, Ms Law.

Thompson May it please the Court, I appear for the respondent liquidators, my name is Thompson.

Elias CJ Yes thank you Mr Thompson. Yes Mr McKenzie.

McKenzie May it please the Court, before I move into my submission there are, I will have to apologise, one or two documentary matters that I will need to trouble the Court with. Unfortunately the documents were settled while I was overseas and it's only in final preparation that counsel discovered that there are one or two matters that I feel it proper that the Court should have included in the material before it. The first is if I could place it before the Court, perhaps I'll give them together to the Registrar so that they can all be handed up together. The first is a notice of originating application. The Court should have that because that is the document filed by the appellant which commenced the proceeding..

Elias CJ Yes thank you.

McKenzie The second is.

Elias CJ Could you just give us a moment to have a quick look at it.

McKenzie Yes.

Elias CJ Thank you. Yes thank you.

McKenzie It might be convenient for Your Honours to place that document in the folder in case on appeal at Tab 5 just in front of Mr Otway's affidavit which would be the appropriate place for it.

Elias CJ Yes thank you.

McKenzie Then the second omission unfortunately is a passage from Derham's text which is at Tab 7 and although there are a number of passages reproduced from Derham, unfortunately those that followed para 13.01 were not included and I place those which could conveniently be put at tab 7 of the list of authorities of the appellant. And Your Honours will see the passage there, 13.01 is included but not the following parts of s.13.

Then the third is s.95 of the Australian Bankruptcy Act. The earlier statute of 1924 to 1930. And that could conveniently be placed with the Australian Bankruptcy Act at tab 4, preceding that Act. I had in my submissions referred to s.122 of the Australian Bankruptcy Act 1966 as the statute where the words, the intent to prefer was replaced by the words relating to the effect of preferring. In fact on further research they first arose under the earlier Australian s.95 and its proper therefore that that be put before Your Honours. It is referred to in the Richardson case (**Richardson v The Commercial Banking Co of Sydney Ltd** (1952) 85 CLR 110) which was the first of the cases, the running account cases. And it arose under that earlier statute.

So I do apologise to Your Honours that there are those supplementary documents to put before you.

I have also prepared some brief points by way of reply which I will refer to in the course of my submission. And some supplementary authorities will be included with the points on reply.

Tipping J Mr McKenzie before you open your substantive submissions, just in the interests for me anyway of getting just a little bit of clarity in one point. Does your client effectively accept that they are caught by s.292 but assert that they can escape if you like through s.310.

McKenzie Exactly Your Honour. Yes. I suppose the nub of the submission is that the appellant says that Homer nodded in this case, that s.310 which the appellants say is central to disposition of transactions relating to set-off was not focused on unfortunately in the Court of Appeal.

Tipping J But you are not suggesting that you can escape otherwise than through s.310.

McKenzie Ah.

Tipping J That's what I'm wanting to.

McKenzie Yes, if that argument were to fail, then the argument that's directed to the running account cases becomes relevant because the appellant says that the Court looked too narrowly at the effect of s.292(2) and should have looked at the whole transaction. So that that is an argument that arises if the appellant is unsuccessful in relation to s.310.

Tipping J I follow thank you.

Elias CJ Mr McKenzie, isn't it more accurately put that there's no preference so there is no application of s.292 on your argument because of s.310.

McKenzie That is entirely correct Your Honour.

Elias CJ Yes, yes.

Tipping J Yes, yes.

McKenzie The nub of the submission is no preference, 292 cannot apply. It's only necessary to resort to 292 if the appellant is unsuccessful in that respect.

Elias CJ Yes.

Tipping J There would have been a preference but for 310.

McKenzie Yes, yes, that would have to be I think accepted.

Tipping J Yes.

McKenzie Preference that might be saved by the later wording of the section. There's one final document if Your Honours do not have enough extra material. But I think that it's one that if Your Honours wish to see I will place before Your Honours. Your Honours will notice that in the supplementary authorities at Tab 5, I've included a comment, a brief comment on the Transotway case before the Court of Appeal made by Dr Andrew Beck. That only became available after the documents were compiled. It's a recent comment. There is one other comment which I have only from the author in the form of a printer's proof. And I do not wish to put that before Your Honours unless Your Honours were prepared to receive it. That is a comment which is shortly to be published in the Journal of Banking and Financial Law and practice. And I can undertake if Your Honours wish to see that comment, to file with the Court the article when it is in fact published. But it contains the proofed version, it will be I understand the article in the form in which it will be published.

Elias CJ I think it would be preferable for you simply to indicate to us where it will be published and I would not like us to get into the position of the Australian Supreme Court which is sent unpublished material regularly. But I'll just take a moment to check whether others have different views on that. No we'd rather not establish a precedent of receiving unpublished material Mr McKenzie.

McKenzie I quite understand Your Honour. Perhaps if I could simply then give Your Honours the journal where this article will appear, I think before the end of the year, it's.

Tipping J Are you suggesting we should wait for it.

McKenzie Not at all Your Honour. It's not of such substance. It simply indicates the views of commercial lawyers on the Court of Appeal decision. I don't think I could say that great weight must be put on the article in that sense at all. It's an article by David Craig to be published in 2005 16 JBFLP which is JBFLP Journal of Banking and Financial Law and Practice. And it's a comment on the Transotway case.

McGrath J And that was at page.

McKenzie Well the page I have is page 1 but it's clearly not page 1.

McGrath J So page to come, page to come.

McKenzie I'll have to check that. Page still to be assigned to it.

McGrath J Right thank you.

McKenzie Yes. I'll move then if Your Honours please to my submissions. As Your Honours will know, this is an appeal from the judgment of the Court of Appeal. Leave have been granted. And there were two approved grounds of appeal which are set out in para 2 of the submission. (a) whether the Court of Appeal wrongly held that the discharge of a debt by way of settle made within the specified period can be regarded as a payment for the purposes of s.292(1)(e), Companies Act. And then (b).

Elias CJ You are not relying on that, you are not advancing anything on that from what you've said in your introduction to us, is that right.

McKenzie Well I would advance that the Court of Appeal wrongly held.

Tipping J What's the purpose of such a submission.

McKenzie That this could be.

Tipping J Because if it wasn't a payment it was clearly a transfer of property. It can't have been a nothing.

McKenzie I'm not suggesting, that was certainly an argument that was advanced before the Court of Appeal. That particular argument is not being pursued given the wording of the agreement, the way in which that was expressed. But the submission here is that the Court of Appeal wrongly held that the transaction here could be regarded as payment for the purposes of that section of the companies act. It does not come, the plaintiff says, does not come within that provision.

Elias CJ I had thought that you said it didn't come within that provision because it wasn't a preference because you're entitled to have set off.

McKenzie Yes, yes.

Elias CJ You are not arguing are you that it was not a payment of money.

McKenzie No, no.

Tipping J No. It's a transaction.

McKenzie That was earlier argued.

Elias CJ Yes.

McKenzie But that's not an argument that is being pursued in this Court.

Elias CJ Yes thank you.

McKenzie Yes, His Honour Justice Tipping correctly described it as a transaction. And I think that would be the more appropriate way of referring to it.

Blanchard J Well it's got to be a transaction because it comes within one of the five criteria or descriptions in subs 1.

McKenzie Yes.

Blanchard J Are you arguing that it's not within (e)?

McKenzie It's not within (e) because of the application of s.310.

Elias CJ But without that it would have been within (e).

McKenzie Yes, yes.

Elias CJ You accept that.

Blanchard J But 310 goes to s.292(2), not to s.292(1). 310 is concerned, or is relevant to the effect, not to whether it was a transaction. Or to what kind of transaction it was.

McKenzie No I'm sorry, did I say 292(1).

Tipping J Whatever it was, it was a transaction which gave your client more than it would have got in the liquidation. Unless you can show that you would have got the same in the liquidation because of the setoff in 310.

McKenzie Yes.

Tipping J I think this is becoming grossly overcomplicated.

McKenzie It may be that the question is not unfortunately well framed.

Tipping J I think what happened was that the Court granted you leave on the questions that were profit, but on more precise analysis they don't perhaps fully and accurately reflect the real issue.

McKenzie They could have been more precisely expressed given the nature of the submission that I wish to put before the Court. If it's necessary to seek leave in order to amend that ground I would be.

Tipping J Oh no, no, no.

McKenzie I would seek that leave.

Elias CJ No, there's no question of that. The questions as framed are intended to make sure that nobody's taken by surprise in what is argued. And that points which would not fall within the statutory criteria for leave are not advanced later. That's really what they're there for, they're for guidance.

McKenzie Thank you Your Honour.

Blanchard J Can I come back to my question. Is it accepted that what occurred was a transaction because it was a payment of money by the company.

McKenzie Yes that, the argument that this was a transfer of property and not a payment is not being pursued in this Court.

Blanchard J It would be difficult to say it wasn't a payment given the history of the section.

Tipping J And the structure of the transaction.

McKenzie Yes and the wording of the agreement. The Court of Appeal did place weight on that.

Blanchard J Well the wording of the agreement really recognised but I suppose one could still have attempted to argue that despite the wording of the agreement it wasn't a payment. But that would I think fall foul of case law prior to 292 and the way in which in the parliamentary process 292 was amended to pick up all the elements of a transaction including a payment by way of setoff it would seem to me, which were absent from the definition of transaction when the bill was first introduced.

McKenzie I would need to accept that in this Court. Although there was an argument earlier advanced, it's not now pursued.

McGrath Mr McKenzie it's the payment of money rather than the setoff arrangement that that was an element of that's a transaction. Is that right on your argument.

McKenzie Well it's a payment of money pursuant to a setoff transaction. A payment that was set off against another payment.

McGrath Yes.

McKenzie However one describes that.

McGrath Well that's the context. But it's the payment of money that the Act focuses on doesn't it as the transaction.

McKenzie Yes, yes.

Elias CJ It does seem to me that this concession that's been made must however cause you great difficulty in your argument based on value. Because if it had been a property transaction then there would have been and to establish what values were exchanged for the purposes of s.310. But if it's a payment of money, you will have to convince me that the Court of Appeal was not correct in saying that it was, they said it was sort of beyond argument or something like that.

McKenzie Is Your Honour looking at the question then whether it constituted a preference.

Elias CJ Yes, yes based on the argument that you do seem to be advancing that the client list wasn't worth the value attributed to it.

McKenzie That, yes, that's an argument that arises only if I'm wrong in relation to s.310 in its application.

Elias CJ I see yes.

McKenzie And I'm driven back then to this then being a transaction under s.292(1) and it's necessary then to resort to s.292 and argue the Court must look at the overall transaction including the way in which the parties came to enter into their agreement and the purpose of that transaction before deciding that the creditor was advantaged.

Elias CJ I see but if s.310 applies, then there's no question, there's no question of any further consideration of value because you have a payment of money as you acknowledge.

McKenzie That's rt.

Elias CJ Yes, thank you.

McKenzie Yes.

Elias CJ Thank you, that's helpful for me.

Tipping J Just one minute, just while we've got a hesitation. It's always seemed to me Mr McKenzie that the key issue in this case subject to 310(2) which is the factual issue is whether you can escape from 292(b), that is whether it enabled you to receive more towards the satisfaction of your debt than you would have otherwise got or likely have got in the liquidation. You say no it didn't because of s.310, because we would have got exactly that in the liquidation had the transaction been executory rather than executed.

McKenzie Yes.

Tipping J That's really what this case is all about isn't it.

McKenzie That's the nub of it Your Honour. That it takes it out of s.292 because of the nature of a setoff there is no advantage.

Tipping J You'd have got the same outcome in the liquidation via 310.

McKenzie Exactly.

Tipping J Provided you can get over 310(2).

McKenzie Yes. And in my submission that's the area where attention should have been focused rather than on 292 itself.

Eichelbaum J Well was that ever raised in the High Court.

McKenzie It was, no, it was certainly raised in the Court of Appeal.

Eichelbaum J Yes.

McKenzie And there was quite extensive argument.

Eichelbaum I know you say that. I was asking about the High Court.

McKenzie But in the High Court as I understand from my friend Ms Law, that was not a factor that was really pursued by the liquidator. The liquidator had not really pursued the question or those issues with Mr Otway.

Eichelbaum But the onus was on your client. The onus was on your client.

McKenzie The affidavit evidence from my client indicated that he had no knowledge, that's what he affirms and that was repeated again before the Court of Appeal.

Blanchard J Well that's not the test. It's a cause to suspect or a reason to suspect test.

McKenzie Yes. And I will submit to Your Honours that there's no basis on these facts for saying that that test was satisfied.

Eichelbaum But that's a factual issue which surely should have been thrashed out and decided before the Associate Judge.

McKenzie Yes as my submissions have indicated Your Honour, it was not, it was not investigated and dealt with by the Court at that earlier stage.

Tipping J You are not saying it was conceded by the.

McKenzie Certainly not Your Honour.

Tipping J No.

McKenzie Certainly not, it was always of course denied by the appellant. But if this Court.

Tipping J Denied by the respondent.

McKenzie Well, Transotway, yes.

Tipping J The liquidators have never conceded have they that you had no cause to suspect.

McKenzie No the liquidators haven't conceded that but neither did they pursue that particular ground or have it resolved by the Court.

Tipping J But it wasn't for them to pursue. You had to show that both tests in 310 were established. 1. That you were entitled to setoff. And 2 you had no cause to suspect.

McKenzie It's a matter that the Court has not determined. And if it's an issue that troubles this Court then the proper course would be to refer the matter back to the Associate Judge for determination. But that issue not yet having been determined.

Tipping J Is that accepted on the other side that that is the proper course or is that going to be the subject of argument.

McKenzie I'm not aware what the respondent's view would be on that issue. I would invite Your Honours to in fact find on the evidence that's before the Court that Transotway, the evidence does not support any view that Transotway had grounds to suspect and make a finding accordingly. But if the Court is not prepared on the evidence, which I would submit to Your Honours is clear on the affidavits we have, if the Court's not prepared to determine the matter, it should be referred back to the Associate Judge.

Tipping J Well what about the question of xxn on affidavits and so on, how are we going to handle that. I presume that no-ones given any attention hitherto to that issue.

McKenzie No, that has not been investigated.

McGrath So you're happy to have the matter decided just simply on the basis of the testing of affidavits by other affidavits.

McKenzie Yes my submission would be that on the affidavit evidence that is before the Court, the appellant is well able to satisfy the Court that there was no basis for his suspecting insolvency in this case using the test that my friend has put forward in the Queensland Bacon case. (**Queensland Bacon Pty Ltd v Rees** (1966) 115 CLR 266).

McGrath You want us to go on to decide the matter so there's a final decision on all aspects.

McKenzie Yes.

Elias CJ Mr McKenzie I can. Sorry.

McKenzie If the Court however were troubled for the reasons that Justice Tipping or was it His Honour Sir Thomas advanced, the absence of testing of that affidavit evidence, then if that troubles Your Honours the appropriate course would be to refer the matter back.

Elias CJ Mr McKenzie I can see some substantial impediments to this Court undertaking the determination that you're suggesting. Because if the matter had proceeded in the High Court on the basis that s.310 was engaged then consideration would have to have been given to whether there would be xxn on the affidavits. Nobody's really had an opportunity to do that because of the way the matter came before the Court. However we've probably interrupted you enough. And we'll let you.

Tipping J It's useful to know where one's headed.

Elias CJ Yes, yes exactly.

Blanchard J We promise to keep quiet for a little while.

Tipping J Yes.

McKenzie Thank you Your Honour. Perhaps if I could just proceed to the summary of the argument and then move to the particular grounds that the appellant wishes to advance. Under Summary of the Argument, (a) a setoff is established it is submitted between the parties by way of an agreement called the March agreement entered into prior to the commencement of the liquidation pursuant to which the appellant agreed to pay to the company a named sum for the company's client list and the parties acknowledged that this constituted full payment of an amount in the same sum owed by the company to the appellant. It is submitted that the Court of Appeal was in error in treating this discharge of the debt by way of setoff as a payment for the purposes of s.292(1)(e) of the Companies Act in that the Court failed to refer to or apply s.310 of the Companies Act which provides for setoff of mutual debts in liquidation.

Blanchard J Well I know I did promise to be quiet. But really, haven't we already established that that's not an accurate statement of your argument.

McKenzie Yes I apprehend that Your Honours put the position on the basis that rather than focus on s.292(1)(e) it's s.292(2)(b) that provides the.

Blanchard J Yes.

McKenzie Avenue through which the setoff provisions can be examined.

Blanchard J Yeah. So you say this is a transaction. It's a transaction of a certain nature. And having established it's a transaction within 292(1) you then look at the comparison between what happened here and what would have happened in the liquidation had the transaction not occurred.

McKenzie I think a detailed analysis of the steps to be taken would perhaps lead the Court there. I would suggest to Your Honours that the Courts generally have, when they've approached this issue, have if you like taken the short cut and have simply asserted as indeed Derham does that where there is a proper setoff, then there is no preference. That is a proposition that is find in the texts and in the cases. So the Courts have simply moved straight through I know without perhaps going through the analysis that Your Honour has done.

Elias CJ I had thought though we'd got to that point really on the oral argument you've advanced to us and I don't understand the respondent's to be disagreeing on that point. So isn't the area that you need to address us on the s.310 application.

McKenzie Yes I too did wonder whether the respondent did not see that there was an issue to confront there. But I'm not sufficiently sure of that to not seek to persuade Your Honours that the view that I've put forward in this respect is correct. But if Your Honours feel that it's not a matter that needs to be pursued at any great length I'm content. But I would wish Your Honours to be satisfied that on the authorities the argument that I'm advancing here is well based.

Tipping J I don't think you need your (b), your point is covered by your (c). It's not a preferential transaction, using the word transaction in the defined sense, because of 310. You lose nothing by abandoning (b). I thought we'd been over all this ground.

Elias CJ That is really what the respondent seems to me to be acknowledging in para 7 of the submissions. That's the summary of them.

Blanchard J That pretty accurately sets out the position doesn't it.

McKenzie Yes I think that that paragraph read on its own, I'm quite content with that. And I think there are other observations in the respondent's submission that made me wonder whether the respondent meant to go that far. But as that paragraph stands, yes I'm perfectly content to see matters framed in that way. And I would agree with Justice Tipping that (c) does what we say is required.

Tipping J If you're not going to get home on (c) nothing else matters.

McKenzie Yes, yes.

Elias CJ What (c) are you referring to?

Tipping J Little (c) in the summary.

Elias CJ Oh right.

McKenzie Then in coming to (d), this is really the alternative ground assuming that the Court was not going along with me in (c) and does find that there is an issue under s.292. Then the submission here is the Court further failed to take into account the scheme and policy of s.310, 292 when considering the meaning of transaction in 292(1) of the Act. Namely the policy that where there is a setoff, prior to liquidation it is inequitable to require a person to pay the full amount of his liability to a debtor and at the same time be confined to receiving a dividend for what the debtor owes him. I take back, that's not an alternative argument. That is simply a restatement as a matter of policy of (c), the underlying policy that supports the way in which the appellant is approaching those two sections.

Blanchard J In other words you're entitled to deal on a net basis.

McKenzie Yes, yes. And that I would submit is fundamental. It's the underlying policy of the provisions here. And perhaps the reason for the sense of concern on the part of commercial lawyers that that might not be recognised.

Eichelbaum J I was inclined to read (d) as providing an alternative ground why this was not within (e) of s.292(1) but I'm obviously wrong in that.

McKenzie It's an argument that's directed to providing further support for the view that where there are mutual obligations, they are to be taken into account in liquidation. And may, as in the facts of this case, extinguish any ongoing indebtedness.

Tipping J Well it's a netting both ways isn't it.

McKenzie Yes.

Blanchard J So you apply s.292 with what s.310 requires in a liquidation in mind and conscious of the policy behind s.310 and indeed behind the law of setoff generally.

McKenzie Yes.

Blanchard J That people are entitled to deal on a net basis.

McKenzie I entirely agree Your Honour.

Eichelbaum J But it doesn't actually have anything to do with the meaning of transaction does it.

Blanchard J No.

Eichelbaum J As per the second line of your (d)?

Blanchard J I think it's this confusion between the argument on 292(1) and the argument on 292(2) which is bedevilling us.

Elias CJ Well for my part Mr McKenzie I don't think there is any argument on 292(1) on the basis that you've put forward today, that you accept this is a payment of money. So then you move on to considering whether there's been a preference applying s.310. Is it more complicated than that?

McKenzie No, I agree Your Honour and I think His Honour Sir Thomas Eichelbaum is quite right that intruding again the words when considering the meaning of transaction in 292(1) of the Act are simply a distraction and I would accept that they should come out.

McGrath So (d) in the end is really just an argument of interpretation in relation to (c).

McKenzie Yes. By reference to the underlying policy.

McGrath Yes.

McKenzie And then (e), I'll come to (e) which is the alternative ground if one does have to look again at 292(2)(b) if the s.310 argument were to fail, that the Court of Appeal was further in error when determining it a payment by way of setoff made within the specified period can be treated as a transaction in isolation from the entire agreement of which it forms a part. The approach taken by the Court runs counter to that expressed in the running account cases in Australia and to the policy of determining preferential effect. The Court should examine all the circumstances surrounding the transaction and not view for example a series of payments in isolation. Now the Court may not get that far.

Elias CJ No.

McKenzie Or need to get that far but if it does then this is an issue of some significance for commercial lawyers in New Zealand. And the Court might wish to say something in that area. I agree that this is a narrowly focused case and one could develop much more extensive argument than I have on the application of the running account cases.

Elias CJ You wouldn't get to them, it's not simply a fall-back is it because if s.310 applies, then is there any scope, but you don't succeed because it's not demonstrated that he had no, Mr Otway had no reason suspect. But if that position is reached then can you go to these running account cases at all.

McKenzie Well one's then, if 310 applies then that provides it's own regime.

Elias CJ Yes.

McKenzie For dealing with the question of.

Elias CJ The netting effect.

McKenzie Of good faith really and knowledge on the part of the creditor. And it has it's own regime for dealing with that.

Tipping J If subs (1) of 310 applies but you can't satisfy (2), there's no further escape via the running account cases.

McKenzie If subs (2), yes I think Your Honour's right.

Tipping J I don't see how you could. As you say it's a regime. You take it for better or for worse.

McKenzie Yes.

Tipping J If it's available to you in concept but not in fact because of your failing to satisfy subs (2), you can't say oh well thanks very much, I'll back off that and I'll go down the running case line. I wouldn't have thought.

McKenzie That's the way I had approached it. Your Honour's raised the question now which had not occurred to me as to whether one could still say okay, if.

Tipping J Well you haven't it argued Mr McKenzie in that form.

McKenzie I haven't argued it.

Tipping J So I don't think it would be fair to the respondent to say. I would read that as a true alternative to 310. In other words, if you don't get into the 310 regime at all, you invoke running account. But if you're in law but not in fact, then I don't think you can invoke the running account regime can you.

McKenzie That had been the way that I had approached it.

Tipping J Well that just confirms what I understand. If you want to try and go further well I'm not trying to stop you. I just wanted to understand

what your stance was. Because with great respect, this summary is a little elusive.

Blanchard J Mr McKenzie I'm in similar difficulty in trying to understand how this argument was intended to fit in. Is it an argument that if you look at the entire agreement, put all the elements of it together, there is no preferential effect.

McKenzie Yes, because it's an argument that arises under 292. And it's really directed to the question in 292(2)(b) on an overall view of the effect of the transaction, has it enabled in this case Transotway to receive more towards satisfaction of its debt than it would otherwise have received or been likely to receive in the liquidation. So that in answering that question my submission is that the Court of Appeal took too narrow a view by focusing on the single transaction narrowly on the setoff arrangement itself and did not look more widely at the background to this, the reasons why the parties entered into that transaction. And whether on an overall view it could be said that Transotway was advantaged.

Blanchard J Well is the argument then that the transaction is the entire, is what happened in all parts of the agreement when you put them together.

McKenzie Yes.

Tipping J It's not a running account argument, it's an argument that you can put, that the transaction has been too narrowly construed.

McKenzie Exactly Sir.

Tipping J I don't know what it's got to do with running accounts.

McKenzie I think, the running account cases are simply referred to as showing a line of authority which demonstrates that the Court is to take this wider approach. Because the submissions I will make are that those cases are based on an underlying principle.

Blanchard J Well can I just ask you then which part of s.292(1) do you say this composite transaction fits into.

McKenzie Well the transaction which is attacked is the arrangements in relation to the payment of money coming under 292(1)(e), the mutual arrangement between the parties. But in looking at that transaction, for the purposes of 292(2)(b) the Court must ask and say well is this transaction avoidable, (a) is satisfied, but what about (b), does it enable Transotway to receive more than it would otherwise have received. That's the issue.

Blanchard J Is that asking the Court to go behind the figures in the agreement.

McKenzie It's asking the Court to look more widely than those figures, to look at why the parties entered into that arrangement. And what the overall advantage to Transotway would be.

Blanchard J But does that not, for you to succeed wouldn't it require the Court to adjust the figures. Because on the face of the agreement which may be all we can look at, on the face of the agreement there is a price for the business which is paid in cash, there's a price for the list which is paid by way of setoff.

Elias CJ And what you acknowledge to be a payment of money.

McKenzie Yes.

Blanchard J And the advantage gained by the setoff on the list still remains.

McKenzie If you do as the Court of Appeal did and simply look in isolation at that setoff arrangement, the extinguishment of the debt as against the value put on the list.

Blanchard J Well I'm not. I'm having regard to the other part of the transaction.

McKenzie Well the other part of the transaction in my submission involves the acquisition by Transotway for a significant sum of money, the assets of this company. An integral part of the transaction was as part of that deal we will pay you the 300 odd thousand dollars if there is this arrangement entered into. There would be no question at all of Transotway entering into that arrangement were they to see themselves in the position of having to pay another nearly $100,000. So that one has to look at the overall nature of the arrangement and ask well did that arrangement at the end of the day advantage Transotway – no.

Blanchard J Look, on the face of the agreement they paid a market price for the business. The 300 thousand odd dollars.

McKenzie Yes.

Blanchard J And at the same time they agreed to pay $94,000 for the list. Which has to be taken as its value. And that payment was not made in cash. It was made by effecting a setoff against an existing debt and thereby it is said there was an advantage.

McKenzie Yes, I submit.

Blanchard J Subject to s.310.

McKenzie Yes, yes. What I'd seek to persuade Your Honours there is that it is an integral part of a wider arrangement. There was a debt for nearly 100.

Blanchard J But aren't you asking us to readjust the value paid for the business. Because in terms of the agreement a market price is paid for the business. 300 odd thousand dollars.

McKenzie Yes.

Blanchard J So we are to look at that figure and say well in fact that's not the real figure.

McKenzie No I think Your Honour is entitled to have regard to fairness aspects here and indeed when you look at the running account cases that element is certainly present. And to look.

Blanchard J Well are we to say the list wasn't worth 94,000.

McKenzie I think what you can say is that Transotway, being owed nearly $100,000 would not have entered into an agreement to pay significant value for the other assets had it seen the position here as being one where it would find itself having to give up in a sense its claim for $100,000. Its giving up of that claim in relation to the value that was placed on the company's client list is part of that wider transaction. And one has to ask whether the transaction looked at as a whole has so advantaged Transotway and in my submission it has not.

Tipping J Well if you add to the 370 the 95, effectively you were paying for the whole shebang 465 weren't you?

McKenzie Yes that's rt.

Tipping J Well now are we being asked to inquire into whether that was a fair price for the whole shebang. Because it's all a question of exchange of values. I have the greatest of difficulty and mystification in that if you've structured the transaction in this way.

McKenzie Perhaps I could put it another way Your Honour. The policy behind the provision and it's been made clear in Australia also in the running account cases and the way in which the Courts have approached those cases, is that in a near insolvency situation, a situation where a co if you like, not known to be insolvent but it's certainly not healthy. Impediments should not be placed in the path of companies and their creditors fm entering into arrangements which are designed to secure or may have the effect of securing the ongoing life of the co. Now the running account cases are clearly an example of that. Someone continues to pay the power bill so that their business activity can continue to receive electricity and continue to operate. But in this case, although it is a single transaction, it's in the context of Newman being an ongoing business securing a reasonable sum for its assets and facilitating that kind of disposal of its assets.

Tipping J When this idea of presenting it in this ingenious form first strike your client. I mean you'd have expected if this was going to be a live issue that the matter would have been properly investigated in at least one of the lower Courts. I may be being wholly unfair Mr McKenzie but it strikes to me that this is just coming fm some, if I may say so, very assiduous attn to your client's best interests, at the final court.

McKenzie It was certainly pursued with some vigour in the Court of Appeal. And I could present Your Honours with the submissions fm both parties that dealt at some length with this issue there.

Tipping J But are you really in effect saying that you want to go behind the way the transaction was structured for whatever reason you chose to get this offset between the debt and the client list. And now you are saying it would have been better if you had had the thing on a more composite basis or if the Court looked at it on a more composite basis.

McKenzie Yes I recognise the difficulty in asking the Court to try and revalue a transaction which parties have themselves negotiated and agreed to enter into.

Blanchard J For tax reasons.

McKenzie Well that was no doubt an element of it and Your Honour will see a reference in the affidavits to that.

Blanchard J Yes.

McKenzie But given that, as a matter of policy I guess, looking at the policy here, if the Court is to take a narrow and focused view as the Court of Appeal did to a transaction of this kind, then it operates to seriously discourage what can be to the advantage ultimately of creditors, disposition of the business to a creditor that's already owed a significant sum of money and is prepared to take the assets at reasonable value.

Blanchard J But look Mr McKenzie, in the running account cases the Court wasn't being asked to rearrange anything. It was simply being asked to allow the parties to deal in a net basis.

McKenzie Well it's also being asked to look at the totality of the transactions and the.

Blanchard J Yes because it would have been artificial not to. But here you're really asking us to regard part of the transaction as a sham. You are really saying, look this client list never ever had any value, it certainly wasn't worth $94,000. And what was really going on was a writing off of Transotway debt. But they did it by giving an artificial value to

the client list and then doing a setoff. That's a sham argument it seems to me.

McKenzie I'd seek to get away fm that aspect of it by simply saying, looking at it in totality, here is a situation where the parties are negotiating for the sale of, well virtually all the assets of the business. Which is not in a particularly healthy state. It discourages parties from entering into any arrangements of that kind where fair value is given if the Court is going to take an isolated, in relation to a setoff arrangement made in the context of that arrangement, a very narrow and isolated view ltd to that transaction and not looking more widely.

Blanchard J Well no I'm endeavouring to look at the whole transaction. But in looking at it I have to take the values as the parties ascribe them. Justice Tipping added the two figures together.

McKenzie Yes.

Blanchard J And then did the what I'll call the before and after comparison. And it still leaves you with a situation where there's been an advantage subject to s.310, because of the setoff. So aren't you then forced to say, well don't treat it as a setoff. Treat it as something different.

McKenzie Yes I wouldn't want to put things in that way. The setoff is there. What I am submitting is that the setoff is an integral part of a much wider transaction.

Elias CJ But as soon as it's an integral part of the transaction, then it seems to me it's very difficult to escape the conclusion that it's a preference to that extent. I mean there may have been occasion to value, to compare values if this had been simply a property transaction. But even then I would have thought the bringing the setoff into play makes it very difficult to ask the Court to reopen that assessment of value. But here you've got what you've acknowledged to be and which the parties structured as a payment of money. It's hard, that's why I said at the beginning, it's hard to see that the Court of Appeal wasn't entirely correct to say it was self-evident that there was a preference to the extent of the debt.

McKenzie If you simply look at the setoff arrangement itself and the payment of value put on the client list in exchange for extinguishing a particular debt then that may be so. But if one asks more widely, has in this case Mr Otway negotiated to secure some advantage for himself in this arrangement then in my submission the answer would be no.

Blanchard J Well if the client list was worth $94,000 and if the business was worth 300 and whatever it was thousand dollars, then he has.

Tipping J He's got his debt paid in full by one means or another. He may be entitled to do so under 310 and escape the preference. But I have to

say Mr McKenzie the idea of trying to rejig all this afterwards to show that he hasn't got repayment of his debt in full.

McKenzie Well.

Tipping J And thus subject to 310, has got a preference, I'm finding it very difficult.

McKenzie Well looking at the wider policy. And perhaps I can't it further than this at this point Your Honour. But if one looks at the wider policy, then if the Court is to take that view of a transaction which is entered into to acquire assets of a co for value as here, significant value, where the co is not in good health, there's always the prospect, even although that may not be in the mind of the person who negotiates, or in the forefront of that person's mind that there could be a winding up situation, commercial people are not going to enter into transactions of that kind and run the risk that the elements a bit later can mean that they can find themselves in the position of having to disgorge.

Blanchard J But how can we view the matter in that way without going behind the figure placed on the client list and saying it wasn't in fact worth that, the parties just put that figure in for convenience.

McKenzie I think, yes I think Your Honour can go this far and say well would the purchaser have entered into a transaction of that kind on the basis that there remained.

Elias CJ Well this is the change of position.

McKenzie An unpaid debt of $100,000.

Elias CJ Well is this a change of position argument? Because that remains to be considered doesn't it? If you say would the purchaser have entered into the transaction.

McKenzie There are some transactions that clearly one can put on one side of the line and say clearly here the purchaser has stipulated for an advantage and secured an advantage at the expense of creditors. No problem at all in the Court requiring the purchaser to disgorge in that circumstance. There are other transactions in which I would put this where when you look at the transaction overall that line cannot be so clearly drawn. And that's where I would place this transaction.

Tipping J Mr McKenzie can I put this to you, calling a spade a spade. The only basis on which you have not received full value for your debt and thus more than you would have got in the liquidation is if the client list was not worth what it was represented to be worth in the transaction. And your client is wanting to argue that that is the case. Because if he cant argue that or doesn't argue that he's clearly got full payment of his debt. And he wouldn't have got it in the liquidation.

How can he escape from the proposition that he's trying to argue one way or another that he didn't get full value for his debt because it wasn't worth, the client list wasn't worth $95,000.

McKenzie I recognise the force of that Your Honour but I can only take Your Honour to looking really at the overall elements if you can put it that way of intention and in terms of fairness in relation to the transaction. And whether it would or could have been said to have been entered into with that kind of advantage being stipulated for. And I would submit not.

Tipping J It's not the intent of the parties any more, it's the effect of the transaction. The effect is to pay your client's debt in full. Simply on the face of this transaction, however you analyse it.

McKenzie Fair weight must be put on the word enabled. Hs it been entered into in a way that's enabled Mr Otway.

Tipping J Its effect enables.

McKenzie To receive.

Tipping J We've got to get away fm this idea of purpose or intent. It's all now focused on effect isn't it. It has enabled your client to have his debt paid in full. There's nothing pejorative in this. It's a simple matter of fact. But the policy is you claw it back unless you can get out of that consequence. You say you can through s.310. And frankly that is your best point.

Eichelbaum You're only point.

Tipping J It's your only point as Sir Thomas says, I agree. I think we're spending a huge amount of time on a dead horse myself.

McKenzie Well perhaps just finally before I leave the point if I could just take Your Honour to the way in which the authorities, if Your Honour were to buy into the Australian view, put the matter in one of the early cases, **Re Discovery Books** (**Re Discovery Books Ltd** (1992) 20 FLR 470). This is at tab 17 of the Appellant's volume. And that's, yes unfortunately I see the page numbers have not come out here. It's the third page in that tab.

Blanchard J Tab 7?

McKenzie Tab 17.

Blanchard J Footnote 7.

McKenzie Yes. That's the only. So the second and related matter which the decision makes clear is that where a payment forms an integral part of

an entire transaction, its effect as a preference involves a consideration of the whole transaction. The fact that a payment made for a time going to reduce an antecedent debt is not necessarily conclusive.

Tipping J But consideration of the whole transaction doesn't mean unpacking the transaction and asking a Court to hold that even as a whole it achieves something that it doesn't on its fact achieve surely. I can understand saying you cant see, you mustn't take an individual aspect of a transaction on its own but you are asking us to unpack this transaction. Unless we do that it's not going to avail your client.

McKenzie Well I don't know that I can take this further Your Honour. Simply to say that creditors on a broader view of the transaction were advantaged by the substantial sum that was paid overall for the assets of these lists.

Tipping J I assume they were worth that. And they would have been worth that in the liquidation.

McKenzie I think that's a very big assumption to make Your Honour.

Tipping J Well I don't think.

Blanchard J But come on Mr McKenzie. We can't get into the business of examining a purchase price, the purchase price for the other assets and saying, well that was a good price or no it wasn't such a good price.

Tipping J Justice Fox can't possibly be meaning in that passage which is supported by footnote 7 that you could sort of rejig the whole transaction. And I'm looking at whether or not it wasn't in part a sham or false values have been placed on certain parts of it. He couldn't possibly have been meaning that.

McKenzie I agree. One can only look at the overall elements of it and ask whether looking overall at the transaction creditors have been disadvantaged or this particular creditor advantaged.

Blanchard J Well yes but you have to accept the values that the parties have attributed to assets in doing that. And in the Australian cases it was simply a series of payments. Nobody was questioning the amounts of those payments. It was a matter of looking at it overall to see what advantage or otherwise there was. But you are asking us to use Justice Tipping's phrase, to unpack the transaction and start making our own assessment of what the values really were. And if we did that, if we said oh well the business wasn't worth 300,000 it was worth 200,000 and the client list was not worth 94,000 it might have been only worth $1,000.00. Yes, once one has done that, one can then do the before and after comparison and perhaps come to the

concern that there's no advantage. But the problem is that I don't think the Court can legitimately go behind the figures that the parties have attributed.

McKenzie Yes well perhaps I've taken that issue as far as I can. If I were to move to page 5 of the submission which deals with the, well perhaps no I can move beyond that. It's to page 7 of the submission to para 19. Perhaps simply to observe there at the start of that submission that I do not understand my friend to now be contending that this was not a matter that was in issue earlier in this proceeding and so it's I think not necessary for me to deal with the points in that para where I seek to make clear that the matter was before the Court of Appeal. And that it's subject to the submission by both parties.

Para 20, the Court of Appeal failed to deal with the submissions that were addressed to it on the application of s.310. It was recognised by the respondents that if a liquidation setoff in terms of s.310 was available to the appellant then the appellant did not receive a preference. The respondent's argument against the application of s.310 turned on whether s.310(2) applied and that's already been a matter of discussion by Your Honour with counsel.

McGrath Mr McKenzie can you just submit more background as to the basis on which both parties dealt with the matter in the Court of Appeal and in particular was the question of whether the parties felt there was a need for cross examination of the deponents on the affidavits.

McKenzie No.

McGrath Were they quite happy to deal with it as if it was a judicial review proceeding for example?

McKenzie No, that really was not adverted to in the Court of Appeal. The parties presented submissions on the basis of the evidence that was put forward in the affidavits which are before this Court.

McGrath And the adequacy of that just wasn't adverted to either by the Bench or by counsel.

McKenzie Not that I understand. I'll ask my Junior and perhaps come back to Your Honours after the adjournment in response to that question. But my understanding, from reading the judgment, is that the parties simply presented submissions on the basis of what was before the Court.

Tipping J But presumably by inference the parties were content for the Court of Appeal if it had addressed or reached the point to decide the factual issue solely on the affidavits.

McKenzie I was not counsel there but the way I read the matter as it was put at that stage would indicate that to me. But I will ask my junior and I know of course that Your Honour may also hear submissions on the point from Mr Thompson.

McGrath The other point I'd like to know Mr McKenzie is whether it was a surprise to the parties that s.310 was not dealt with or whether there was some signal by the Court of it's preliminary view of s.310 that explains why it wasn't dealt with.

Blanchard J It's a surprise to me.

McKenzie It was a surprise to me also. I will raise that question with my Junior as to whether anything was expressed in the course of the hearing on that point. My understanding is no but I would want to be clear on it.

McGrath Thank you.

McKenzie Yes Mr Thompson said that he could confirm that and perhaps he could confirm that also to Your Honours.

I then refer to a passage from Derham, this is in para 22. And it's possibly not necessary to take Your Honours in detail.

Elias CJ I don't think there really is any issue about this Mr McKenzie.

Blanchard J It's summarised neatly in that quote from Washington Diamond Mining that you've got at the bottom of your page 9 (**Re Washington Diamond Mining Co** [1893] 3 CH 95).

McKenzie Yes and I perhaps can emphasise the point where the emphasis has been added to the quote from Derham in para 24 where the reference there is to the parties agreeing that cross-demands should be set off one against the other and cancelled. If I can observe there, there appears to have been a misunderstanding on the part of the Court of Appeal that the transaction here being the way the Court of Appeal approached it, the setoff arrangement, the parties having entered into that agreement that without more brought it within the provisions of s.292 with the consequences that followed.

Blanchard J That would be very odd wouldn't it.

McKenzie It does seem odd.

Blanchard J It'd be better to just be silent and allow the law of setoff to govern so that when settlement came along one party said, oh I'm entitled to a setoff.

McKenzie If I could just perhaps take Your Honour to the passage where it seems to me the Court of Appeal may have been under that

misunderstanding. There's first of all at para 28, this is at Tab 2, the case on page 10 and the second sentence there. Transotway did not agree to take the claim … satisfaction of the debt. On the contrary, Transotway expressly agreed what it would pay for the client list and the parties further expressly agreed that two payments would be set off. So that is acknowledged. And then where one comes to paras 34, 35, the court is dealing there with a passage from Derham where it's believed that counsel had not understood the text in context. And if I could just perhaps pick up at the latter part of 34. That is not a debate we need to enter. However as the setoff in this case did not arise as a result of a prior agreement committing the creditor to act unilaterally to set off mutual money obligations as between it and the debtor. The passage there was dealing with this type of arrangement, a unilateral resort to a fund. The power of setoff in the present case arose from the parties' entry into the March agreement. The setoff in this case was not a unilateral act by Transotway. And then there's further reference to Derham.

And then I pick up where their Honours say in the very next sentence, he contrasts that situation, that's the unilateral resort to a particular asset, with the position we have in the present case. On the other hand the circumstances surrounding the incurring of the debts subject to the setoff with the entry into the setoff agreement itself could give rise to a preference. And I think their honours in my submission misunderstood Derham at that point. And saw that as indicating that an agreement to enter into a setoff, a setoff agreement in itself gave rise to a preference. And that perhaps is at the heart of the Court of Appeal's difficulty. In my submission that's clearly not so. Very frequently parties agree to enter into a setoff arrangement and that is as much subject to s.310 as the case where there are simply mutual obligations.

Blanchard J You are not, and this is a side issue I'm raising, you are not advancing the argument that Derham appears to advance that setoff doesn't involve a payment by the debtor.

McKenzie That was earlier advanced. It's not being pursued in this Court. I don't think it's necessary for the Court to get into that level of analysis in relation to these transactions.

Blanchard J Well I don't want to encourage you too much because I'm not myself convinced by what Derham says. But if it isn't a payment by the company, then arguably it's not a transaction and s.292 doesn't apply.

Elias CJ But it's conceded in this case that it's a payment of money.

Blanchard J Yes, I know, but I'm just wanting to make absolutely sure that Mr McKenzie is not being misled by the Court to jump over a point.

McKenzie I think the difficulty that the appellant faces here is the nature of the agreement that was entered into and the acknowledgement that formed part of that agreement.

Blanchard J I think that's right.

McKenzie So that was a point earlier taken. But it did seem to me that it was a difficult point to sustain on these facts.

Blanchard J Yes. It also would be very difficult I think when you look at 292(1) in its entirety. It's so all-embracing that it includes amongst a transaction an acceptance by a company of execution. In other words the execution takes place and the company doesn't do anything about that. If something of that nature is regarded as a transaction, it would be very unusual I think if a setoff were not regarded as a transaction. And in case law prior to s.292 where the same elements were present in the statute, setoff has been regarded as something that can be a preference.

McKenzie Yes.

Blanchard J So it seemed to me that with the greatest of respect to Dr Derham, that view did not seem to be correct.

McKenzie Yes well I think Your Honour's observation is an interesting one. In another case it's one that perhaps could be examined further. But given the nature of the agreement here it did seem to me that, for the particular difficulties Your Honour's mentioned, that generally that that might not be a line that could be pursued.

Blanchard J Well they called what occurred a payment.

McKenzie Yes that's the difficulty.

Blanchard J But it's not whether it was a payment that we're considering at the moment but whether it was a payment by the co. The argument being that it's something compelled by the creditor who insists on setoff.

McKenzie Yes' that's not situation here. Yes.

Tipping J It was a consensual setoff here wasn't it.

McKenzie Yes.

Elias CJ But I think the point raised is appropriate that there are subtleties here that we would need to be fairly careful about which don't really arise because of particular facts here, the form of the agreement and the acceptance that what happened here was a payment of money by the company. Am I wrong in that because that. So that frankly Mr McKenzie, it seems to me that there is no help but to close in on

s.310(2) and that it seems to me where the respondent is at in the submissions we have.

McKenzie Yes.

Tipping J Para 84 of the respondent's submissions, although not absolute, seems to almost concede that you're entitled to invoke 310 but they resist you on the basis of 310(2). The submission says, 310 would arguably have operated to set the purchase price etc. So it says arguably have operated.

McKenzie Yes.

Tipping J Well frankly I would have thought it was very close to unarguable. But he takes his stand on subs (2). So I for myself, subject to any resiling from that that may come from the respondent which would seem highly unlikely, no he's shaking his head quite rightly, I don't know what all this argument's about.

McKenzie Well given that view, I think I can reserve perhaps for any reply that might be needed.

Tipping J Oh yeah, if he, but he's not going to, he's just shaken his head. He accepts that you're entitled to 310 I think effectively.

McKenzie Well that being the case, I don't think it's necessary then for me to pursue. The remaining argument that I've brought in relation to the application of s.310, where that does bring us of course is to the application of subs (2) and that's dealt with in paras 30 and the following paras that Your Honours have already very fully taken me through.

Tipping J Well if we're to decide it I would want to hear you in detail. But the real issue is whether we're going to decide it or whether we're going to send it back to the High Court.

McKenzie Yes.

Tipping J And frankly I would, with respect, think perhaps that might be the best thing to look at next. Whether we're going to decide it or whether it goes back to the High Court. Because if it's going to go back to the High Court we don't want to hear you on the detail.

McKenzie Well perhaps if I could indicate to Your Honours the nature of the evidence that was before the Court so that at least Your Honours are aware of the issues.

Tipping J Well what is the attitude of the respondent to who's going to decide it. If both of you want us to decide it that would be one thing. If there's a difference of view on it well then one would want to hear

argument on that point before embarking into the detail of the evidence.

McKenzie Yes well maybe that can be left for the reply also. The appellant's position there is that the appellant would be content for this Court to deal with that issue on the basis of the evidence that's before the Court, namely the affidavits that are contained in the case, on the basis of that affidavit evidence.

Elias CJ Well perhaps it may be convenient to take the adjournment now and perhaps you could confer with Mr Thompson as to what the attitude of the respondents is because that may help you in terms of how you address s.310(2) to us.

McKenzie Thank you Your Honour.

Elias CJ Thank you Mr McKenzie.

Court adjourns 11.28 am
Court resumes 11.52 am

McKenzie Yes, just dealing with the two matters that were raised before the adjournment. Ms Law says that the written submissions before the Court of Appeal raised the issue of s.310 although the respondents countered in their submissions by saying, oh this hadn't been raised it was claimed in the originating application at an earlier stage. Nonetheless themselves presented reply submissions in writing on s.310. So the issue was before the Court. But the interchange that took place between the Court and counsel was largely oral and the Court in that interchange focused substantially really on the question that there was a payment under s.292(1)(e) and on the issue whether the liquidator was entitled to pick and choose from elements of a larger transaction. Could the liquidator simply claim to set aside the receipt of the debt. The payment that was made on account of the debt and not deal with the other aspects of the setoff arrangement. And as Your Honours will see, the Court of Appeal in its judgment held that the liquidator was entitled to pick and choose in that way. That may have some implications of course for an argument under s.292(2) although the way the Court's then focusing on that is it may not get to that point.

So really what I'm coming to there is that s.310 was before the Court. It was at no stage indicated by the Court that one way or the other how it viewed s.310 and its focus was on other issues, with no suggestion that the Court was not going to deal with s.310.

Tipping J And the whole of 310.

McKenzie Yes. But it was just not a matter that was focused on in the interchange between the Court and counsel as I understand it.

Tipping J But the parties were content in the Court of Appeal for the Court to deal with all aspects of 210 including the factual point.

McKenzie 310, yes.

Tipping J 310.

McKenzie Yes.

Tipping J Including the factual point.

McKenzie Yes which was covered by both parties in their written submissions. Both went into the evidence before the Court on the affidavits.

Blanchard J And no-one suggested to the Court of Appeal that the 310 (2) question should be referred back to the Master.

McKenzie No things never got to that point. So that the appellants.

McGrath J Well when you say it never got to that point. Wasn't it really the situation that implicitly both parties were happy to proceed on the basis that cross-examination wasn't required and they'd just deal with it on the affidavits.

McKenzie That's my understanding of the way in which both parties approached that issue in their submissions. Both dealt with it.

McGrath J And nothing to the contrary was ever raised or suggested and it proceeded accordingly.

McKenzie That's right.

McGrath J Before the Court of Appeal.

McKenzie Not that the Court of Appeal, to be fair, actually in interchange brought up the issue. But it was there before it in the written submissions.

McGrath J I think we're problem more concerned with the parties than the Court on this aspect.

McKenzie Yes, yes.

McGrath J And the parties were content to deal with it on the papers before the Court.

McKenzie Yes. That's my understanding.

Blanchard J And has the respondent suggested to you that it's no longer happy?

McKenzie No. In fact the indication is that the respondent is happy.

Blanchard J Right.

McKenzie For this Court on the basis of the evidence before the Court, namely the affidavit evidence to deal with that issue. The respondent maintaining of course that the onus is on the appellant to satisfy the Court in terms of s.292(2). The appellant.

Blanchard J Did you mean 310.

McKenzie I'm sorry 310(2). I'm sorry. The appellant also is content for this Court to deal with that issue. Again on the basis of the evidence before the Court in the affidavits.

Tipping J And your key point there is your client's statement in his affidavit that he had no knowledge of the insolvency, is that the position.

McKenzie That's not the only point.

Tipping J No, no.

McKenzie But it is in my submission a significant point because he was not cross-examined. There was no cross-examination on the affidavits. That was not challenged and that evidence therefore remains uncontested before the Court.

Tipping J What para is that Mr McKenzie.

McKenzie Yes, if we come to para 31 of my submissions.

Tipping J I'm sorry, of the affidavit I meant.

McKenzie Oh the affidavit, it's in para 16. And it may be appropriate just to take the Court through that affidavit evidence at this stage. And tab 5 is Mr Otway's affidavit. And perhaps Your Honours might like to look at para 4 briefly refers to the nature of the agreement, the March agreement entered into in broad outline. Para 5, the prior dealings, mutual dealings between the parties leaving an outstanding balance. Para 6 the March agreement. Sorry in March the issue of a statutory demand and that's particularly relied on by my friend Mr Thompson. We'll deal with that. And at the same time para 7 show's the parties were negotiating for the sale of the assets. It's significant, the second sentence in para 7, on Monday 24 March Lesley Newman came to see me and proposed the Plaintiff buy him out. So the approach came from the company to Transotway. And then there's the negotiation. And a refusal to put value on goodwill. Whereas Your Honours will see that Mr Newman considered that there was goodwill and was holding out for some value there.

Para 8 is significant. When I was negotiating to purchase Newman I asked Mr Newman for a copy of its financial statements but he would not supply them and I did not press the point.

Tipping J I wonder what inference one might draw from that.

McKenzie It's covered by Mr Newman later in his affidavit and perhaps I'll come to that Sir. Well no it's really covered here. Yes, he says as far as I was concerned I was taking over Newman's assets and Newman's history of trading was irrelevant. So that he was not particularly concerned about its trading history, he wanted the assets. And I would suggest to Your Honours that that was not an uncommercial approach to take where the other party to the transaction was not providing financial stmts.

Then there's reference to the agreement in principle. And at para 10, describes the way in which the setoff arrangement came to be negotiated. Para 13.

Tipping J Just before you move on, this arrangement whereby the deponent was prepared to have assigned to it a price far higher than the real value, he was thereby in effect saying really that he wasn't getting anything for his debt or very little. Therefore one might be inclined to infer that he knew that this guy was going to go bung and he wasn't going to get anything anyway.

McKenzie No I submit that would not be a fair inference at all to put on the negotiating. Your Honour needs to.

Tipping J I'm just putting it to you Mr McKenzie.

McKenzie Yes.

Tipping J Because it just seemed to me to be a possible inference. And we're being asked to try a point of fact here.

McKenzie Yes, yes. I would suggest to Your Honour that in the preceding paragraph it's clear that Mr Newman is holding out for $200,000.00 of goodwill. He wants on top of the figures given for the assets that they were negotiating, he wants $200,000.00 more.

Tipping J Mm, but why is Mr Otway going to, well value a debt at a figure, or put a price on the debt at its true value but knowing that actually he's not going to get anything near true value for.

McKenzie Well the way that I read that evidence is that in the end he comes in effect close to $100,000.00 to what Mr Newman is wanting for goodwill.

Tipping J But he doesn't think goodwill's worth anything.

McKenzie He doesn't think it's worth anything. He's still owed $100,000.00.

Tipping J So he pays $100,000.00 for goodwill.

McKenzie And he's prepared to put in this extra $100,000.00 as Your Honour earlier observed, the total transaction therefore being over $400,000.00 in value. And to avoid negative tax consequence it's done in this particular way.

Blanchard J That pretty much destroys the earlier argument you've made. So it's just as well we're concentrating on s.310.

McKenzie I thought Your Honour might have made that point. And I don't, yes I don't want to go back there. But at this point of the argument, what this does indicate is that there were commercial reasons, however one views them, for structuring the transaction in a particular way but they're not reasons from which one can infer knowledge of insolvency. There are other reasons, not the reasons that His Honour Justice Tipping was earlier suggesting as possible, other reasons for doing it this way. And I think one has to accept that yes Mr Otway didn't see a lot of value in the client list.

Tipping J But he's giving up an asset prima facie worth $95,000.00 in return for a worthless asset.

McKenzie Yes because if he's going to acquire the assets at all, there's some goodwill factor being sought by Mr Newman and he's not going to pay him $200,000.00, he's very reluctant to pay him anything but at the end of the day it's done this way to give Newman $100,000.00 more in effect.

Blanchard J Was there a restrictive covenant.

McGrath J Yes.

McKenzie Yes I believe there was yes.

McGrath J Yes.

Blanchard J So he effectively buys the client list, gets a restrictive covenant, he's paying for goodwill.

McKenzie I expect you can see it in those terms. It was structured a different way.

Blanchard J Yes. Which means there was definitely a preference in relation to the setoff. Subject to s.310.

McKenzie As I said I rather not go there Sir. But for the purposes of this argument I think it indicates a commercial approach to their negotiation and the way in which this was achieved. To give more value at the end of the day to Mr Newman. And yes, the paragraphs there, then 13 dealing with what Mr Otway considered to be the lack of value in the client list. And says, Newman's debt to the plaintiff, para 13, would be wiped which I was willing to agree to because the plaintiff had Newman's operation. At the end of the day he wanted the operation and that's what he had to pay Mr Newman to get it. There's no inference in my submission of any motivation there in terms of a doubtful solvency situation.

And then para 16 is important. A few weeks after the agreement was entered into Newman went into voluntary liquidation. Had I known the companies true financial position which the directors did not disclose I would never have agreed to their demands that the agreement record an inflated value for the customer list to clear the debt.

Elias CJ That seems to be an acknowledgment that it would be a preference.

Tipping J Quite.

McKenzie It's an acknowledgement that he had some recognition that he would be disadvantaged in insolvency. It would be an imprudent form of transaction for someone to enter into where the company was insolvent or believed to be financial very precarious.

McGrath J There's nothing here stated about the place that the winding up notice has in all of this. There's no explanation of what was intended, how that was intended to fit in …

Blanchard J The statutory demand.

McKenzie Oh the statutory demand.

McGrath J The statutory demand, yes, yes.

McKenzie Yes, that is covered and one might say by.

McGrath J It's in the reply affidavit was it?

McKenzie Yes it's stronger evidence so far as Mr Otway's concerned in terms of any onus because it comes from Mr Newman. And also Mr Otway's affidavit in reply which I'll come to. But if we looked at Mr Newman's affidavit at tab 10. I'm sorry. Tab 9. And Your Honours will see the history of the negotiation set out in the earlier paragraphs. An acknowledgement of the amount that was owing. Although there was disagreement as to how much.

Blanchard J Wasn't it a bit odd that the amount that Mr Newman was prepared to admit was owing wasn't being paid and hadn't been paid for two years.

McKenzie There'd been an ongoing dispute between the parties.

Blanchard J But only as to quantum.

McKenzie Yes.

Blanchard J And according to this affidavit Newman thought the true figure that he ought to be paying was $68,000.00. Well wasn't it, didn't it look a bit odd that that figure wasn't being paid when it was an undisputed debt.

McKenzie I'd submit Your Honour that there were mutual, the parties have indicated that there were a series of mutual dealings between them and that the amount that was actually owing was a matter of some contention between them. But not that that would have necessarily created any inference in Mr Otway's mind given the mutual nature of the relationship that the failure to discharge at least that part that might be indisputably owing was not made. But paragraph 7 does show that by March 2003 a statutory demand was made.

McGrath J So you're at paragraph 7 of Mr Newman's affidavit.

McKenzie Yes that's right. Your Honour will notice that that confirms that it was Mr Newman who proposed selling his business. Made the approach. And in relation to the statutory demand, by the time Transotway's statutory demand for payment of $94,000.00 was served negotiations were already under way between me and Mr Otway for the possible sale. Mr Otway's file note records a discussion between us. Exploratory discussions had already taken place before then. So he's suggesting that there are ongoing discussions. Disagreement as to goodwill. And then paragraph 10 is the significant one about the statutory demand. And Your Honours will notice that Mr Newman states that it was to gain leverage in our negotiations.

Tipping J This reference to cash flow difficulties Mr McKenzie.

McKenzie Yes.

Tipping J I know there's an explanation for why there were cashflow difficulties. But the very fact that you were having cashflow difficulties which is a nice sort of accountancy sort of expression for not being able to pay your debt, would be rather significant wouldn't it in this context.

McKenzie Taken on its own such a statementt might be. But one needs to couple that with the fact that what Mr Newman is saying to Mr Otway is, or explaining, slowness in payment and this may well have also indicated why Mr Otway wasn't getting paid so promptly, was a change in our accounting systems meant that some of our customers were slow to pay us.

Tipping J Yes but that's not quite my point.

McKenzie And Mr Otway thought.

Tipping J My point is it doesn't really matter why you're insolvent, it's the fact of insolvency that's the key point. Now here he's saying he's having cashflow difficulties which in effect means you aren't able to pay your debts when they fall due.

McKenzie With respect no Your Honour. The cashflow difficulties are because your accountants are putting in a new system which is making it difficult or inefficient for you to make the payments that you otherwise would. He's blaming, rightly or wrongly, the accounting system.

Tipping J No, but no he's not.

McKenzie Not a lack of liquidity if Your Honour pleases.

Tipping J No if you read the sentence he says he's experiencing cashflow difficulties because of a change in our accounting systems which meant that some of our customers were slow to pay us. Not which inhibited us from paying our creditors.

McKenzie Yes Your Honour's correct in that respect. But I think it's the accounting systems that are the impediment here and causing the cashflow problems. There's no suggestion that the cashflow difficulties are due to liquidity.

Tipping J Well cashflow difficulties is a lack of liquidity.

McKenzie Well due to solvency factors.

Tipping J Yes alright thank you.

McKenzie Yes I think it would be going very far indeed to put onto Mr Otway some obligation to suspect insolvency and given the high level, reasonably high level that's put by the Court in the Queenland Bacon case that I'll come to, as to the basis of that suspicion. So that at the top of the next page, in summary, yes he refers to another offer that they had which he found less attractive. And I won't read all of the affidavit to you but Your Honour there is nothing in that affidavit to indicate that Mr Newman himself thought that the company at this

time was facing insolvency let alone made any statements to Mr Otway to that effect.

In coming to paragraph 16. In the final analysis Transotway agreed to pay $465,000 odd for newman carrying's operation and of this amount there's a reference to the amount paid for tangible assets and the amount he regarded as being goodwill in the form of the customer list. For reasons earlier indicated I think that's again significant.

Then paragraph 23 which deals with the company going into liquidation. And Your Honours will notice that he says the decision was prompted by the sale of the business. Although it had subsequently become apparent that the company was insolvent. He refers to it subsequently becoming apparent. I think those words are significant.

He then deals with Mr Otway's statement that if he'd known of the company's financial position he would never have agreed to their demands etc. He says it's correct that I did not specifically tell Mr Otway that Newman carrying was insolvent. When I was negotiating the sale to Transotway, I was not myself aware of this fact. All the same I told Mr Otway that cashflow difficulties were a motivating factor in my decision to dispose of the business. And that stmt earlier indicates the context in which that remark was made to Mr otway and in my submission it would be wrong to construe that as any admission of insolvency or solvency difficulties on the part of Mr Newman.

McGrath J Is it fair to infer that Mr Otway new of and was using the cashflow difficulties to assist getting to an agreement and used the technique of serving a statutory demand to assist in that regard. In other words the statutory demand was served because he knew that there was the cashflow difficulties in the Newman Company and that pressure would be brought to bear to get an agreement if the demand was served and that's why it was served.

McKenzie Yes I think that that's covered in part in paragraph 10 where the reference is made to the cashflow difficulties because of the change in accounting systems. And then the statement I believe that Mr Otway thought that the statutory demand would pressurise me into giving way on the subject of the price I wanted for goodwill. It's not suggested that that was done to ginger up the accounting system or get ahead of the queue if you can put it that way. And we're not told the sequence of conversations here. Whether Mr Otway was informed of the cashflow difficulties before or after the statutory demand was issued.

Tipping J Mr McKenzie I have some difficulty in reconciling the fact that one serves a statutory demand yet at the same time is asserting that one has no reason to suspect that the company's unable to pay it's debts

as they become due. It seems to me that a service of a statutory demand is prima facie evidence that you are of the view that the company is unable to pay its debts as they become due because that is the very consequence which you're wanting to establish by the failure to fulfil the demand. It is then presumptively unable to pay its debts isn't it. So how can you say on the one hand I can genuinely issue a statutory demand, I'm not doing that as a sham or for improper purposes. But I have no reason to suspect that the addressee of my demand was unable to pay its debts as they become due. I have great difficulty in seeing how one can assert both things contemporaneously.

McKenzie Your Honour the issue of a statutory demand cannot in itself I would submit be taken as evidence of knowledge of the insolvency of the company. It is frequently a means of commercial pressure put on a slow payer to discharge its obligation.

Tipping J I don't want to appear naive Mr McKenzie I know that. But it's not insolvency, I know, it's a type of insolvency, it's an inability to pay debts as they become due. That's what s.310 subs (2) is referring to. It's not a sort of balance sheet insolvency, it's a cashflow type insolvency that we're talking about here. And here we are, here's a man who's told we're having cashflow difficulties, serve a statutory demand but at the same time he asserts that he had no reason to suspect that the company was unable to pay its debts as they fell due.

McKenzie Well in response Your Honour number one we do not know whether Mr Otway was informed of the cashflow difficulties before the statutory demand was issued. That was issued on 20 March and negotiations took place on 23 March. I think it would be fair to infer the discussions about the cashflow problems did not take place until after the statutory demand had been issued. But secondarily Mr Newman whose evidence surely must be the best evidence on this matter, he volunteers the info and he states as a party without interest in this issue, that the statutory demand he believes was served to put pressure on him in the negotiation. And that is an understandable and quite explicable reason for, commercial reason for issuing a statutory demand in this sort of context.

Tipping J Well that's his impression of Mr Otway's motivation. But Mr Otway hasn't told us has he, anything about it.

Blanchard J He has actually.

McKenzie Yes.

Blanchard J In paragraph 7 of his reply affidavit.

Tipping J Oh we've got a reply have we.

McKenzie Yes I was coming to that.

Tipping J I'm sorry.

McKenzie Yes it's dealt with in the reply.

Tipping J I beg your pardon, sorry. I didn't realise.

McKenzie Perhaps we should move to that now.

Tipping J What does he say.

McKenzie Yes paragraph 7.

Blanchard J I decided Mr Newman was not genuine and was simply stalling. In other words stalling on paying the money.

McKenzie I understand that sir in terms of the negotiations. Because the preceding paragraphs are dealing with that.

Tipping J Here's a second occasion. I was unaware that it was insolvent. It's a second occasion where he studiously denied something which is not the statutory question. What would one infer from that Mr McKenzie. In both his first affidavit he said I did not know.

McKenzie Yes.

Tipping J And here he says I was unaware. Which is not the statutory question.

Elias CJ But however he may, it's not entirely proper for him to address the statutory question because that's a matter of inference from all the surrounding circumstances. And perhaps all he can do is say that he did not know.

McKenzie Yes, yes.

Tipping J Well.

Blanchard J He says he didn't know but he then.

Tipping J Yes well that's a charitable view of it.

Blanchard J That is sandwiched between Newman not being genuine and simply stalling. Instructed solicitors to issue the statutory demand. And then a few lines further down in para 9, it was clear Newman wasn't going to pay the money it owed. Well there he's saying he doesn't think that in response to that demand he's going to get paid. If that isn't cause for suspected insolvency I don't know what is.

McKenzie Well there may well be other reasons for that. Given the discussions that were taking place between the parties. Mr Newman holding out because he's wanting more in terms of the purchase price. He's clearly not going to pay over money to Mr Otway at that point in time until the negotiation's concluded. He's only throwing money away in his mind were he to do so. So in my submission there are entirely commercial explicable reasons from the way in which this matter developed that don't suggest any grounds on the part of Mr Otway to suspect insolvency.

And perhaps I should take Your Honour to the way in which the Court in the Queensland Bacon case which is in my friend's list of authorities deals with that matter. It's at tab 6. This is also a running accounnt case and there are observations on that issue.

Tipping J Is this the reference to the passage from the judgment of Mr Justice Kitto.

McKenzie Yes. That's at page 303. Cited by my friend. There's the suspicion that something, that's mid page, that something exists is more than a mere idle wondering whether it exists or not. It's a positive feeling of actual apprehension or mistrust amounting to a slight opinion but without sufficient evidence. Consequently reason to suspect that a fact exists is more than a reason to consider or look into the possibility of its existence. I think it's something which in all the circs will create in the mind of a reasonable person in the position of the payee an actual apprehension or fear that the situation of the payer is in actual fact that which the subs describes. Mistrust of the payer's ability to pay his debts as they become due and of the effect which acceptance of the payment would have as between the payee and other creditors.

Tipping J Well the second half of that is not part of our test is it. It's just the first half.

McKenzie Yes. And if I could look at where his honour discusses the facts at page 305 about two thirds of the way through the passage there. Where he's dealing with the fact that there was a dishonoured cheque in issue here. Looking at the whole picture as he then saw it, with its emphasis on expansion and the fact that the cheque of 10 October had been honoured as the bank had forecast in a week would have projected the idea of insolvency and would have concluded that he had no reason at all for suspicion on the point. He would I think have regarded the episode of the dishonoured cheque as having been due to some temporary difficulty which had been quickly overcome and which there was no reason to suggest was symptomatic of a general inability still existing to pay debts as they became due. So that despite there being an episode of a dishonoured cheque there, there were other factors that the Court considered could quite properly be brought into account.

Elias CJ This Mr McKenzie though was a very long standing debt. And the dealings between the parties have ended in 2001.

McKenzie Yes.

Elias CJ It's hardly comparable is it.

McKenzie It's comparable in this sense that the parties are now in negotiation. They've had their past disputes about how much was owing and that may or may not, and in my view one can't infer from that the level of suspicion that's required, may or may not have been due to difficulties on the part of the company. The matter is now in focus and there are other and quite explicable reasons for the entry into this transaction and any suspicion on Mr Otways part that it was insolvent. And Mr Newman's evidence supports that. Mr Otway himself says it would have been quite uncommercial of him to have entered into the kind of setoff arrangement he did if there had been a suspicion of insolvency.

And then perhaps I could direct Your Honour also to Chief Justice Barwick's judgment at page 281. And the passage there in the para at the latter third of the page which deals with the evidence before the creditors.

Tipping J In each case His Honour accepted the evidence given on behalf of the creditor that the creditor did not know and did not in fact suspect.

McKenzie Yes.

Tipping J That the company wasn't able to pay its debts.

McKenzie But if one looks at the narration there are a series of matters there that one might think could indicate otherwise but the Court is not prepared to take things at that lower threshold. The Court is looking for, as the direction of His Honour Justice Kitto indicates, something more than a bare suspicion here.

Tipping J Mm.

McKenzie And if I could also refer Your Honour to one case in the list put fwd on behalf of the appellant. And that's the **Hamilton v Commonwealth Bank of Australia** ((1992) 9 ASCR 90) Tab 11 at page 113. Where just in a short observation about the Queensland bacon case which I've just referred to, the judge says, I accept that queensland bacon show as that it's insufficient that the circs give a reason to suspect that the debtor might be insolvent. They must be such that the creditor should have suspected that the debtor was insolvent.

And that given Mr Newman's evidence that he did not consider at the time of the negotiations that the company was insolvent, it would be going very far indeed in my submission to suggest that Mr Otway had the necessary, or that the evidence was there that Mr Otway should have suspected that the compnay was insolvent at that time.

So that it is the appellant's submission on this particular issue that the onus is satisfied. That statements in the affidavit should be accepted. They were not challenged or tested. And indeed they are supported where it matters, in my submission, by what Mr Newman as a witness without interest on the matter, what Mr Newman has said. There just is not evidence before the Court that should lead the Court to take the view that Mr Otway at the relevant time suspected that the company was insolvent.

I don't propose to take Your Honour over again the remaining submissions that deal with the running account cases. I could analyse in some detail the Chatfield case which is not in my submission a satisfactory decision at all on this point although it's the New Zealand authority dealing with it. (**Chatfield v Mercury Energy Ltd** [1998] 8 NZCLC 261645. Not only for the reason that I mention in the submission but there are a number of other difficulties in my submission with the way in which Justice Randerson dealt with the issue. If Your Honours wish to hear me on that I could develop that argument but it's perhaps not necessary to take Your Honours' time on that issue.

I just observe because I myself, and I can understand how His Honour came to confuse the sequence in Australia, their sequence of insolvency legislation is not easy to follow, and I had wrongly expressed the view to Your Honour at paragraph 49 that it was s.122 of the Australian Bankruptcy Court 1966 that constituted the radical departure and introduced the effect rather than intent proven. In fact it's the earlier Act that I've put before Your Honour, the 30 statute that made that departure and the earlier Richardson case in 1952 which is in the bundle is the earlier authority on the issue was decided under that earlier statute.

If Your Honours do wish to look at the issue, the critical case to examine there is Tab 15 of the appellant's authorities, the **Dye v Peninsula Hotels** case. (**V R Dye & Co v Peninsula Hotels Pty Ltd (in liq)** (1999) 32 ASCR 27). That's the case that provides support for what *Morison* (*Morison's Company and Securities Law* para 63.7) has to say and it deals in some detail with the sequence of Australian provisions. And expresses the view that the policy and indeed the intent of those provisions is not changed from the earlier statute thru to the current statute which now contains an express subsection dealing with running accounts. The view taken in that case is that that does no more than restate what was already the rule. So that if Your Honours wished to pursue that issue then the Dye v Peninsula

Hotels case is a very helpful authority in supporting what is said by Morison.

Just further, I just draw attention to the points by way of reply. And again I don't propose to go thru all of those. If I could just speak briefly to one or two matters in that additional submission put before Your Honours this morning. The first submission on the date for taking account really I don't think very much turns on that given our statutory provisions now and maybe I'm being somewhat pedantic and I've provided Your Honours with clear authority for the proposition that it's the actual date of liquidation, not any possible relation backdate that is in issue. But I don't understand my friend to disagree with that.

Elias CJ It seems unanswerable.

McKenzie Yes. Your Honours may find some assistance in an interesting case that I came across in that context but which also has a discussion of s.310 and that was the Commissioner of Inland Revenue v Smith case which is in the supplementary bundle. And there's a brief and helpful statement on s.310 at the conclusion of that judgment.

Your Honours as far as the policy of the decision is concerned, would also find help in Guy v McIntyre High Court which is in that bundle also.

I've already dealt really in oral interchange with Your Honours with the submissions under payment by the company. On the submissions relating to the basis for measuring preferential effect I'm not clear to what extent this submission that my friend spends some time on advances his argument and I may reserve for reply any comment on those two differing approaches in the Australian legislation. It does not in my submission appear to assist one way or the other on these facts.

The meaning of the expression, reason to suspect I've already dealt with. Bilateral netting agreement I simply wish to draw attention here to the fact that the appellant does not pursue paragraph 15, the alternative ground put forward in paragraph 38 that the March agreement comes within the definition of a bilateral netting agreement under s.310(a). That's not pursued. The appellant does rely on s.310.

All that those arrangements or statutory arrangements I referred to for the purpose of showing that an agreement, contrary to what perhaps one may infer from the Court of Appeal's approach, that an agreement to net transactions or set transitions off comes within s.310 quite clearly. And it's not limited simply to mutual obligations outside of agreement.

And the running account cases have already been the subject of interchange between Your Honours and me and I don't propose to pursue that argument here.

So that if Your Honours please concludes the arguments on behalf of the appellant.

12.44 pm

Elias CJ Thank you Mr McKenzie. Mr Thompson, I wonder whether you could simply confirm for us that your argument, that on your argument the case turns on s.310(2).

Thompson It does indeed ma'am. It turns on s.310(2). However, there is also an issue, and I can very briefly summarise it, which deals with the sort of running account case points that my learned friend makes. The specific language of s.292(2)(b) doesn't connote any element of a necessity that there be a detriment to the general body of creditors. The language just deals with the matter of whether or not the preferred creditor got a preference. Paragraph 43 of the judgment of the Court of Appeal which has been criticised by my learned friend, arguably, although I have sought in my submissions to make its impact wider, but arguably it contends for that narrow focus simply upon whether or not the transaction that has been attacked produced the result of conferring a preference in the sense of enabling the person to get more in the liquidation than he would otherwise have got. It doesn't deal with detriment.

Blanchard J If he gets more others will get less.

Thompson Well that stands to reason Your Honour. But in my submission all that the cases such as Dye and Co say, the running account issue is in my respectful submission a bit of a red herring because this is not an ongoing relationship type matter. So the import of the running account cases is simply this, does one look at the whole transaction when one is assessing preferential effect, not when one is identifying what the transaction but when one is assessing preferential effect.

Elias CJ Does it matter in this case.

Thompson Well that's my further submission Your Honour. My further submission is that it doesn't matter in this case because if you take the narrow focus, you look at the payment by way of setoff and once you've satisfied yourself that that's a payment of money it satisfied the debt. On the narrow focus approach, the creditor has received a preference. On the bigger picture approach, as a comment from the Bench earlier, a purchase of the whole shebang I think the expression was.

Tipping J Sounds like me Mr Thompson.

Elias CJ It was.

Thompson Thank you Your Honour. Then we have an agreement to pay a gross $465,000.00. Net 371 paid. Preference arises that way. So whether you, it's an important question potentially in some other case.

Elias CJ Yes.

Thompson But it doesn't make one whit of a difference in my submission to the outcome of this matter. So that would be my submission on that. I would have one further small submission to make and that relates to the payment of money by the company. Now as I understand Derham, the issue there, and I understand as well that this is the point of distinction with CIR v Smith, the issue there is where a creditor, for example a bank, exercising a right to combine accounts or somebody like that or the CIR under a statutory right of setoff, unilaterally sets an amount of money that it owes to the debtor off against an amount owed to it by the debtor, that cannot be said in any sense to be a payment by the debtor. It's a unilateral act by the creditor. However, the factual situation we are faced with here is entirely distinguishable in my respectful submission. Here we have a mutual, an agreement to effect a setoff. And therefore that is very much an act by Newman carrying and therefore very much a payment by Newman carrying if one accepts that it is a payment.

Tipping J So the difference is between a voluntary act if you like and an involuntary consequence.

Thompson Yes. Even so Your Honour. As His Honour Justice Blanchard mentioned, it's by no means clear that Derham has got that right. There are cases for example where, and I forget the precise case but I could find it, it's referred to in one of the Australian cases referred to by my learned friend. In fact I think it's referred to in the Hamilton v Commonwealth Bank case. There's an old case referred to there where the conclusion was that the deposit of money by an account holder to one account and the subsequent transfer by the bank of money from that account to cover a debit in another account held by the account holder, amounted to a payment by the account holder because you had to look at that entire sequence of events as in effect the transaction.

So it's by no means clear that Derham is right in that analysis. But in my submission, and particularly to deal with the issue raised by CIR v Smith, that is the point of distinction.

On the evidence, I really don't want to go into too much detail because I think if you'll allow me this latitude I can really wrap up quite quickly now. Really the king hit if you like is the fact that Mr Otway said, he didn't expect to get paid anyway and it didn't matter

what value was ascribed to the debt because he wasn't going to get it so if it had been $10 or it could have been $200,000.00, it didn't matter. In my respectful submission the onus is on Mr Otway. It's not appropriate to look too closely at Mr Newman's affidavits where they conflict with what Mr Otway says. The issue is based upon what Mr Otway himself says, whether he had reason to suspect. And given that he was the director and shareholder of the company his mind must be imputed to be the mind of the company.

There's just one final point which goes to the matter of my learned friend's submission on the sequence. My learned friend submitted that there was nothing to show that Mr Newman had told Mr Otway that by the time the statutory demand was issued that the company was in cashflow difficulties. I'd like to take you to paragraph 10 of Mr Newman's affidavit, that's tab 9 and it's page 106.

It reads as follows: before I had the opportunity to prepare a proposal to submit to Mr Otway however, Transotways statutory demand was served on Newman carrying. I firmly believe that Mr Otway timed this event in order to gain leverage in our negotiations. I had explained to Mr Otway, I had explained to Mr Otway, that one of the reasons I wanted to dispose of the Newman carrying business was because the business was experiencing cashflow difficulties. Apart from stating dates, in my submission there can be no clearer statement of the fact that Newman had told Otway before the statutory demand was issued that the company was experiencing cashflow difficulties. I would respectfully endorse comments from the Bench to the effect that the test is not insolvency as such, it's an inability to pay debts and that the reason for the cashflow difficulties is somewhat irrelevant.

Blanchard J Paragraph 7 indicates that by the time the statutory demand was served, negotiations were already under way. So you're saying, when Mr Otway in paragraph 10 talks about I had explained, he.

Thompson We're referring to earlier discussions. I'm not saying it necessarily happened on the 12th of March which is a meeting referred to in paragraph 8 but.

Blanchard J Well you would expect that if somebody is going to give the reason why they want to sell, they'd be giving it at the beginning of the negotiation.

Thompson Yes.

Blanchard J Which he says is before the 20th of March.

Thompson Indeed Your Honour. Unless there are any other particular issues on which the Court would like to hear me, those are really, that really cuts to the nub of what I have to say. I would like to make a brief

submission on costs. I submit that costs should follow the event in the normal course. However, if the Court were to find against the liquidators, I would submit that there should be an indication on the costs order that the costs be met from the assets of the company. In view of the fact that the position regarding costs is ordinarily speaking the liquidator is not personally liable for costs if proceedings are commenced in the name of the company. But otherwise ordinary principles apply and it's over to the liquidator as to whether the liquidator's entitled to be indemnified by the company or not. However, in the case.

Tipping J Unless we forbade it he would be entitled wouldn't he to indemnify, or they?

Thompson Well he would Your Honour. But in this particular case, in the case of a notice under s.294, the Act specifically requires the liquidator rather than the liquidator in the name of the company or rather than the company to issue the notice. So the liquidator has no alternative in exercise of his statutory function but to become party to the proceedings and named personally. So it's for that reason that I ask for that.

I would also submit that if the matter was to go against the liquidators some recognition should be given to the fact that my learned friend has very late in the date withdrawn his s.310 (a) to s.310(o), the netting agreement argument and after I had spent at least a half a day's research and preparation time which is reflected in my submissions dealing with that. Unless there's anything else Your Honours, those are my submissions.

12.55 pm

Elias CJ No thank you Mr Thompson. And I'd like to say that I found your written submissions admirable and very helpful. Which has no doubt enabled you to be admirably brief in your response. Thank you.

Thompson Obliged ma'am.

Tipping J Yes so did I Mr Thompson.

Thompson Obliged Sir.

Elias CJ Yes Mr McKenzie do you want to be heard in reply.

McKenzie Yes well I think that Mr Thompson has clarified the position that was taken by the liquidators so far as s.310 is concerned. And the issue before the Court really is the application of s.310(2) so that really the Court can approach the matter on the basis that the respondent accepts that on the facts of this case apart from 310(2), s.310 would

remove this transaction from constituting a preference and from attack under s.292.

That being so, then we really only have s.310(2) to focus on and again it's not necessary for me I think to get drawn into the matter I'd earlier mentioned to Your Honours. That is the debate in my friend's submission as to the time at which you look at the impact on liquidators, whether the hypothetical time for the transaction or the date of liqiudation. It really it seems to me doesn't advance matters under s.310(2).

The evidence that my friend most strongly relies on is for him the statement in Mr Newman's affidavit. The second reference to the cashflow difficulties, this is at Tab 9. But that must, that' in para 23, that must be looked at in my submission both (a) in the context of paragraph 7, I'm sorry paragraph 10, where Mr Otway explains, I'm sorry Mr Newman explains what he'd said to Mr Otway, that cashflow difficulties were because of the change in our accounting systems etc.

Blanchard J Well it's more than just that. It's that they're not getting money in from their customers.

McKenzie Yes.

Blanchard J So they're not going to be able to pay their creditors.

McKenzie But that's.

Blanchard J It doesn't matter what the cause of that was. It's the factual situation that they didn't have enough money to pay their creditors that is critical.

McKenzie It's a question of timing I would submit to Your Honour.

Blanchard J I mean it might have been because their customers had all died and there were holdups in getting money out of their estates. It still would produce a situation of insolvency.

McKenzie It would be going far in my view to suggest that Mr Otway ought to have drawn that form of conclusion from what was said to him on that issue. And given the other factor that I wish to emphasise and that is that Mr Newman himself refers to the fact that he, in the same context in para 23, I was not myself aware of this fact, that is that Newman carrying was insolvent.

Tipping J Are you saying in effect he wasn't aware of the fact that he was unable to pay or his company was unable to pay his debts as they fell due. Well.

McKenzie He was aware of accounting, that there were difficulties with his accounting system. And it was not delivering in the way it should have. He's not in my submission saying on the basis of that that I believed therefore that our co was insolvent. To the contrary he denies that. And given that evidence and the absence of any testing of Mr Otway's evidence it would be going very indeed in my submission for the Court to hold that Mr Otway had the level of suspicion that's referred to in the Queensland bacon case on these facts.

He has in my submission discharged the onus that lies on him under the section.

Elias CJ Mr McKenzie I was just thinking, on the point that you were making about the lack of availability of the accounts. And it may be that there's no evidence of this before us, but was this the sole business of this company.

McKenzie That I.

Elias CJ The transportation business. I don't think there is evidence of that before us and I had rather assumed not. But it just occurs to me that your emphasis on the fact that he hadn't seen the accounts might cut the other way. Because if he was purchasing only the assets that might be an indication that the operation of the business was not something that he was acquiring because it wasn't going very well. It may be that there isn't enough info there but.

McKenzie Yes, that would be inferring a suspicion of insolvency in my respectful submission at a very low level of what could be regarded as suspicion. In commercial transactions of this kind it's not at all uncommon for a purchaser, particularly of a small business, to prefer to acquire the assets and not have to make any inquiry into the business's liabilities position. There may be contingencies with the Inland Revenue, very common situation, or other types of contingency that a purchaser simply does not want to get into. It would be going very far to suggest knowledge.

Elias CJ Yes.

McKenzie Or suspicion of insolvency there. That, if Your Honours please, concludes the matters of reply.

Elias CJ Thank you Mr McKenzie. And you didn't want to be heard on the issue of costs.

McKenzie Well so far as that issue is concerned, it would be my submission that in the event that the appellant is successful on this appeal, that the appellant should be awarded costs not only in this Court but also in

the Court of Appeal. The appellant having been put to contest in that Court also and it's appropriate that costs in both Courts be awarded.

Elias CJ Yes thank you.

McKenzie As Your Honour pleases.

Elias CJ Thank you, well thank you counsel for your assistance. We'll take time to consider our decision.

Court adjourns 1.04 pm