SUPREME COURT OF QUEENSLAND

CITATION:	*Adams v Zen 28 Pty Ltd & Ors* [2010] QSC 36
PARTIES:	**JOHN ADAMS** (applicant) **v** **ZEN 28 PTY LTD ACN 124 670 275** (first respondent) and **GEORGE TECK GUAN LEE** (second respondent) and **NATIONAL AUSTRALIA BANK LIMITED** **ACN 004 044 937** (third respondent)
FILE NO:	9588 of 2008
DIVISION:	Trial Division
PROCEEDING:	Application
ORIGINATING COURT:	Supreme Court of Queensland
DELIVERED ON:	16 February 2010
DELIVERED AT:	Brisbane
HEARING DATE:	4 August 2009; 5 October 2009; 14 October 2009
JUDGE:	Daubney J
ORDER:	**1. On the application for summary judgment, there will be orders that the claims against the first respondent and the second respondent be dismissed.** **2. In the second respondent's application concerning the undertaking, there will be an order that the undertaking of the second respondent in the order pronounced by Daubney J on 3 February 2009 to provide a bank guarantee from the National Australia Bank Ltd in the amount of $377,635.96 be henceforth discharged.** **3. I will hear the parties as to costs in respect of these applications.**
CATCHWORDS:	PROCEDURE – SUPREME COURT PROCEDURE – QUEENSLAND – PROCEDURE UNDER RULES OF COURT – SUMMARY JUDGMENT – where decision made by adjudicator appointed under *Building and Construction Industry Payments Act* 2004 in favour of applicant against first respondent – where applicant commenced the present

proceeding by filing an originating application seeking specific relief against first respondent – where undertakings were given by which the applicant refrained from enforcing the judgment debt and proceedings were adjourned – where consent order signed by parties' solicitors whereby an undertaking was given by the first and second respondents to provide a bank guarantee and by the applicant to provide a withdrawal of a caveat upon delivery of the bank guarantee – where the first respondent company went into voluntary administration under Part 5.3A *Corporations Act* – where creditors of the first respondent approved a Deed of Company Arrangement – whether the applicant is a "secured creditor" within the meaning of s 444D(2) of the Corporations Act – whether the terms of the Deed of Company Arrangement can affect the applicant's rights to realise or otherwise deal with his security

EQUITY – GENERAL PRINCIPLES – EQUITABLE DOCTRINES AND PRESUMPTIONS – SUBROGATION – where the applicant is one of several unsecured creditors of the respondent – where the respondent is subject to a deed of company arrangement – where the respondent has rights of indemnity as trustee to which the applicant seeks to be subrogated – where the applicant is the only unsecured creditor to have commenced proceedings to enforce its right of subrogation – where the equitable remedy of subrogation is discretionary – whether the remedy of subrogation would be granted in circumstances which would advance the applicant ahead of other unsecured creditors to their detriment

PROFESSIONALS AND TRADES – LAWYERS – DUTIES AND LIABILITIES – UNDERTAKINGS – where undertaking given in terms of consent order signed by the second respondent's solicitor - where, by a further interlocutory application, the second respondent has applied for orders that the undertaking be discharged – where the second respondent asserts he did not give instructions to his solicitor to give this undertaking on his behalf – where the solicitor confirms that he did not advise the second respondent that an undertaking in that form could impose a personal liability on the second respondent – where the solicitor did not appreciate that the undertaking could be read as requiring a personal guarantee – whether the solicitor did have actual authority to give an undertaking – whether the second respondent ought to be discharged from the undertaking

Building and Construction Industry Payments Act 2004 (Qld) s 31
Supreme Court Act 1995 (Qld) s 47
Corporations Act 2001 (Cth) Part 5.3A, s 444D, s 444H, s444F

Boscawen v Bajwa [1996] 1 WLR 328, applied

Custom Credit Corporation Limited v Ravi Nominees Pty Ltd (1992) 8 WAR 42, cited
Di Mella v Rudaks (2008) 102 SASR 582, cited
Hardoon v Belilios [1901] AC 118, cited
Lerinda Pty Ltd v Laertes Investments Pty Ltd as trustee for the AP-Pack Deveney Unit Trust [2009] QSC 251, applied
Marginson v Ian Potter & Co (1976) 136 CLR 161, cited
Nolan v Collie (2003) 7 VR 287, cited
Octavo Investments Pty Ltd v Knight (1979) 144 CLR 360, cited
Orakpo v Manson Investments Ltd [1978] AC 95, cited
Re Enhill Pty Ltd [1983] 1 VR 561, distinguished
Re Suco Gold Pty Ltd (1983) 33 SASR 99, cited
Re Trivan Pty Ltd (1996) 134 FLR 368, applied
Ron Kingham Real Estate v Edgar [1992] 2 Qd R 439, applied
Spies v The Queen (2000) 201 CLR 603, cited
Trautwein v Richardson [1946] ALR 129, cited
Vacuum Oil v Wiltshire (1945) 72 CLR 319, cited

COUNSEL: On the application for summary judgment:
M M Stewart SC for the applicant
D R Cooper SC for the first and second respondents

On the second respondent's application concerning the undertaking:
M Liddy for the applicant
D R Cooper SC for the second respondent

SOLICITORS: Mills Oakley Lawyers for the applicant
Hynes Lawyers for the first and second respondents
Brian Bartley & Associates for Mr Nickless on 14 October 2009

[1] In August 2008, an adjudicator appointed under the *Building and Construction Industry Payments Act* 2004 ("*BCIPA*") made a decision in favour of the applicant against the first respondent to the effect that the amount of $504,411.82 was due by the first respondent to the applicant. On 5 September 2008, an adjudication certificate in respect of that decision was issued. That adjudication certificate was then filed in this Court pursuant to s 31 of the *BCIPA*, which relevantly provides:

> "(1) An adjudication certificate may be filed as a judgment for a debt, and may be enforced, in a court of competent jurisdiction."

[2] On 26 September 2008, the applicant commenced the present proceeding by filing an originating application which sought, inter alia, the following relief against the first respondent:

> "(1) A declaration that the First Respondent's interest in the whole of the land contained in Instrument of Title Reference 50726315 being more fully described as Lot 2 on Survey Plan No 215488 County of Elphinstone, Parish of Coonambelah ("**the Land**"), is subject to an equitable mortgage in favour of the Applicant such mortgage being

in terms of the Trust Deed contained in registered instrument dealing number 710790806 ("**the Zen 28 Trust Deed**").

(2) A declaration that the Land stands charged with the payment to the Applicant in the sum of:

(a) $504,411.82 together with interest pursuant to Section 47(1) *Supreme Court Act* 1995 (Qld) (or alternatively pursuant to section 67P of the *Queensland Building Services Authority Act* 1991 (Qld) ("**QBSA**") at the rate of 16.43% per annum) upon the whole of such amount from 5 September 2008 until the date of judgment or earlier payment.

(b) The costs as assessed (or otherwise agreed upon) as payable by the First Respondent in the Supreme Court proceedings 8782/08 at Brisbane by virtue of the order made on 12 September 2008 in such proceedings."

[3] It is unnecessary for me to recite further the terms of the originating application, as filed, because on 3 February 2009 it was ordered, by consent of the parties, that the remaining paragraphs (other than as to costs and ancillary relief) be withdrawn.

[4] The originating application was mentioned before the Court on several occasions in late 2008, at which time undertakings were given by which the applicant refrained from enforcing the judgment debt and the proceedings were adjourned from date to date.

[5] The matter eventually came on before me again on 3 February 2009, at which time the following form of consent order signed by the parties' solicitors was tendered to me, and the following orders made:

"UPON THE UNDERTAKING of the First and Second Respondents to provide a bank guarantee from the National Australia Bank Limited in the amount of $377,635.96 to the Registrar of the Supreme Court of Brisbane (to remain with the Registrar until further order) by 10 February 2009.

UPON THE UNDERTAKING of the Applicant to provide a withdrawal of caveat 711925715 capable of immediate registration (upon delivery of the above bank guarantee).

IT IS ORDERED BY CONSENT THAT:

1. The within proceedings be placed upon the Supervised Case List.

2. The Applicant, First Respondent and Second Respondent provide a joint report to the Supervised Case List manager by 4.00pm on 10 February 2010.

3. The parties have liberty to apply on two business days' notice.

4. Paragraphs 3, 4, 5, 6, 7, 8, 9, and 10 of the Originating Application filed 26 September 2008 be withdrawn.

5. The costs of the within proceeding follow the costs in the Supreme Court proceeding 9612/08."

[6] The caveat referred to in the undertakings was a caveat lodged by the applicant on 16 September 2008 over land owned by the first respondent by which the applicant claimed "an equitable estate or interest in the fee simple as equitable mortgagee of the property for the sum of $504,411.82 (together with interest accruing)".

[7] On 10 February 2009, the second respondent, who was the sole director of the first respondent, resolved that Zen 28 Pty Ltd ("Zen 28") was insolvent and further resolved to appoint voluntary administrators under Part 5.3A of the *Corporations Act* to administer the affairs of the company. Jason Bettles and Susan Carter were appointed.

[8] On 17 March 2009, the creditors of Zen 28 met and approved a Deed of Company Arrangement ("DOCA"). Mr Bettles and Ms Carter were appointed deed administrators.

[9] Clause 7 of the DOCA provided:

> "7. **THE EFFECT OF THE DEED ON CREDITORS**
>
> *7.1* ***Release of Claims***
>
> Subject to the rights of Credits to participate in a Dividend pursuant to this Deed, upon execution of this Deed, all debts or claims, present or future, actual or contingent, due or which may become due by the company as a result of anything done or omitted by or on behalf of the company before the day when the administration began and each claim against the company as a result of anything done or omitted by or on behalf of the company before the day when the administration began are extinguished.
>
> *7.2* ***Deliver Form of Release***
>
> Creditors shall accept the dividends paid under this Deed in full satisfaction and complete discharge of all debts or claims which they have or claim to have against the company as at the initial appointment and each of them will, if called upon to do so, execute and deliver to the company such forms of release of any such claim as the Administrators require.
>
> *7.3* ***Prohibition on Recovery Action***
>
> Subject to Section 444D of the Corporations Act, this Deed may be pleaded by the company against any credit not holding a registered security over assets of the company, in bar of any debt or claim that is admissible under this Deed and an unsecured creditor (whether the creditors debt or claim is or is not admitted or established under this Deed) must not, before the termination of this Deed:-
>
> a) take or concur in the taking of any steps to wind up the company,
> b) except for the purpose and to the extent provided in this Deed, institute or prosecute any legal proceedings in relation to any debts incurred or alleged to have been incurred by the company before the initial appointment,

c) take any steps (including any step by way of legal or equitable execution) in any proceedings pending against or in relation to the company at the initial appointment,
d) exercise any right of set off or cross action to which the creditor would not have been entitled had the company be wound up as at the initial appointment, or commence or take any further step in any arbitration against the company or to which the company is a party.

7.4 ***No Release from Subordinating Creditors or Bank***

The provisions of Clauses 7.1, 7.3 and 8.1 do not apply to:-
(a) those subordinating creditors named at Item (vii) in Schedule One; or
(b) the Bank with its secured mortgage."

[10] The DOCA also required that certain deeds of agreement and release be obtained from specified creditors which had agreed to subordinate their claims, particularly the second respondent and other companies associated with the second respondent. The DOCA was executed by Zen 28 and the necessary deeds of release were executed by the subordinating creditors on 20 March 2009.

[11] The appointment of the administrators to Zen 28 had the effect of vacating it from the position of trustee of the Zen 28 Trust. On 10 February 2009, pursuant to the terms of the Trust Deed of the Zen 28 Trust, Glee Storage Pty Ltd was appointed trustee of that trust. It is uncontentious that until 10 February 2009, Zen 28 was the trustee of that trust pursuant to the Trust Deed dated 6 July 2007. (I note, in passing, that this date of 10 February 2009 is mistakenly, and incorrectly, recorded in the DOCA as 10 September 2008. It seems uncontentious that this is an error in the DOCA).

[12] It is not in issue that the applicant did not vote in favour of the DOCA.

[13] The applicant thereafter lodged a proof of debt with the administrators of the DOCA. Material filed by the DOCA administrators reveals that the applicant had an admitted proof of debt in the sum of $389,137.17, and a dividend was paid to him in respect of that admitted proof of debt of $9,731.07 in June 2009.

Application for the claim against the first respondent to be dismissed

[14] The first respondent has applied for the claims against it to be dismissed. The bases for this application are:

(a) that there are overwhelming discretionary grounds for refusal of the discretionary remedy of subrogation, namely that the applicant has admitted that the transaction upon which the adjudication decision, and hence the judgment, was based was a sham;

(b) that in any event, the intervention of the administration of the first respondent company renders the proceeding against the first respondent futile.

[15] For its part, the applicant contends, in brief:

(a) that the contract on which the adjudication and judgment were based are unaffected by fraud, there has been no application to overturn the adjudication, and in any event this issue is res judicata; and

(b) the applicant is a "secured creditor" within the meaning of s 444D(2) of the *Corporations Act*, and the terms of the DOCA cannot affect his rights to realise or otherwise deal with his security.

[16] It is convenient to deal first with the argument concerning the impact and effect of the DOCA.

[17] As appears from the terms of the relief sought in the originating application, the applicant's contention is that land registered in the name of the first respondent as trustee for the Zen 28 Trust is charged in favour of the applicant as a security for its judgment debt. The applicant submits that Zen 28 incurred the liability in the form of the judgment debt to the applicant, that Zen 28 had a right to be indemnified out of the trust assets in respect of that liability, that Zen 28 had a lien or charge over the trust assets to enable it to enforce that right of indemnity, and that the applicant is entitled to be subrogated to the trustee's right to be indemnified out of the assets trust and subrogated to the trustee's lien or charge securing that right of indemnification, to the extent of the debt incurred in discharge of the trustee's duties as trustee. By this process it is argued that the applicant is a "secured creditor" of the first respondent.

[18] Section 444D of the *Corporations Act* provides:

> "**Section 444D EFFECT OF DEED ON CREDITORS**
>
> **444D(1) [Deed binds creditors]**
>
> A deed of company arrangement binds all creditors of the company, so far as concerns claims arising on or before the day specified in the deed under paragraph 444A(4)(i).
>
> **444D(2) [Realisation of securities]**
>
> Subsection (1) does not prevent a secured creditor from realising or otherwise dealing with the security, except so far as:
>
> (a) the deed so provides in relation to a secured creditor who voted in favour of the resolution of creditors because of which the company executed the deed; or
>
> (b) the Court orders under subsection 444F(2).
>
> **444D(3) [Owners and lessors of property]**
>
> Subsection (1) does not affect a right that an owner or lessor of property has in relation to that property, except so far as:
>
> (a) the deed so provides in relation to an owner or lessor of property who voted in favour of the resolution of creditors because of which the company executed the deed; or

(b) the Court orders under subsection 444F(4).

444D(4) [Creditors becoming members]

Section 231 does not prevent a creditor of the company from becoming a member of the company as a result of the deed requiring the creditor to accept an offer of shares in the company."

[19] Section 444H of the *Corporations Act* provides:

"**Section 444H EXTENT OF RELEASE OF COMPANY'S DEBTS**

444H A deed of company arrangement releases the company from a debt only in so far as:

(a) the deed provides for the release; and

(b) the creditor concerned is bound by the deed."

[20] The first respondent submits that the applicant is bound by the DOCA and that, by operation of cl 7 of the DOCA, the claim against the first respondent in reliance on the judgment debt is extinguished. The applicant, however, contends that he is a "secured creditor" within the meaning of that term in s 444D of the *Corporations Act*. It is uncontentious that he did not vote in favour of the DOCA and no order has been made by the Court pursuant to s 444F(2). The applicant submits, therefore, that if he is a secured creditor, the terms of the DOCA cannot prevent his rights to realise or otherwise deal with his security.

[21] Maintenance of the claim against the first respondent turns, therefore, on whether the applicant is a "secured creditor" for the purposes of s 444D.

[22] Many of the issues argued and agitated in respect of the claimed status of the applicant as a secured creditor were discussed by McMurdo J in *Lerinda Pty Ltd v Laertes Investments Pty Ltd as trustee for the AP-Pack Deveney Unit Trust*.[1] In that case, the applicant was a creditor seeking termination of a Deed of Company Arrangement. The company was a fruit and vegetable wholesaler. The applicant was one of its suppliers. The company was insolvent by the time it ceased to carry on its business in November 2008, when the business was transferred by the directors to other companies they controlled. A week later they appointed administrators to the company. A meeting of creditors later voted in favour of a Deed of Company Arrangement, which was executed in January 2009. The company carried on its business as trustee. The applicant creditor contended that, because the trustee was insolvent, it was entitled to be subrogated to the trustee's rights of indemnity against the trust assets. The creditor submitted that, if the DOCA stood, it would be unfairly prejudiced because of the minimal dividend it would receive from the administration, in circumstances where it was otherwise entitled, it claimed, to be subrogated to the trustee's right of indemnity in full out of the trust assets.

[23] It is appropriate for me to quote at length, and respectfully adopt, the following observations and statements by McMurdo J:

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1 [2009] QSC 251.

"[4] The company incurred its liability to the applicant, as it did to its other creditors, in the discharge of its duties as a trustee, and therefore has rights of indemnity. A trustee is entitled to apply trust property directly in satisfaction of its liabilities as a trustee (a right of exoneration) and to reimburse itself from trust property where it has discharged a liability from its own funds (a right of recoupment).[2] To enforce the indemnity, a trustee has a charge or right of lien over the whole range of trust assets except for those, if any, which under the terms of the trust deed may not be used for the carrying on of the business. There are thereby two classes of persons having a beneficial interest in the trust assets, the first being the beneficiaries for whose benefit the business was being carried on, and the second being the trustee. The trustee's interest will prevail over that of the beneficiaries.[3] Where the trustee is insolvent, a creditor of the trust may be subrogated to the trustee's rights of indemnity and in particular to its lien or charge securing that right of indemnification.[4]

[5] The applicant argues that it is thereby a secured creditor of the trustee but that the DOCA would treat the property over which it has that security as available for unsecured creditors. It is argued that the applicant is entitled to enforce its security directly against the assets of the trust to the extent of discharging its debt in full. By this means the applicant claims to have bypassed the queue of the company's creditors who, according to the administrators,[5] would receive eight cents in the dollar under a liquidation.

[6] The question which immediately arises is how it could be that the applicant has gained that advantage over other creditors. The debts owing to them were incurred in circumstances no different from those of the applicant's debt. The difference, the applicant seems to argue, is that it has taken steps to enforce its right to subrogation. It did so by these proceedings, commenced by an originating application on 3 November 2008, prior to the appointment of the administrators. The originating application claimed a declaration that the whole of the property of the trust was charged in favour of the applicant for the payment of its debt and the appointment by the court of persons to enforce that charge by taking possession of the trust property. By the same originating application, it sought an order to wind up the company on the ground of insolvency. But none of those orders has been made. The applicant instead has since filed and prosecuted this application to terminate the DOCA.

[7] Subrogation is a remedy, not a cause of action: Orakpo v Manson Investments Ltd;[6] Boscawen v Bajwa;[7] Re Trivan Pty Ltd;[8] DiMella v Rudaks.[9] In Boscawen, Millett LJ said:

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2 *Octavo Investments Pty Ltd v Knight* (1979) 144 CLR 360 at 367.
3 Ibid.
4 Ibid at 367-8; *Vacuum Oil v Wiltshire* (1945) 72 CLR 319 at 335-6; *Ron Kingham Real Estate v Edgar* [1999] 2 Qd R 439 at 443.
5 In their report under s 439A of the *Corporations Act* 2001 (Cth).
6 [1978] AC 95 at 104 (Lord Diplock).
7 [1996] 1 WLR 328 at 335 (Millett LJ).
8 (1996) 134 FLR 368 at 372-3 (Supreme Court of New South Wales).
9 (2008) 102 SASR 582 at 590.

> "Equity lawyers speak of a right of subrogation, or of an equity of subrogation, but this merely reflects the fact that it is not a remedy which the court has a general discretion to impose whenever it thinks it just to do so. The equity arises from the conduct of the parties on well-settled principles and in defined circumstances which make it unconscionable for the defendant to deny the proprietary interest claimed by the plaintiff. A constructive trust arises in the same way. Once the equity is established the court satisfies it by declaring that the property in question is subject to a charge by way of subrogation in the one case or a constructive trust in the other."[10]

In *Re Trivan Pty Ltd*, Young J said that:

> "The next matter that should be noted about subrogation is that it is really not a right, but a remedy, that is, it is a remedy which a court of equity will grant in order to prevent there being an unconscionable situation …
>
> Furthermore, it is an equitable remedy. That means that it will not be granted merely as a right, but will only be granted in circumstances where it is appropriate to do so."[11]

[8] The applicant's case assumes that the equitable remedy of subrogation would be granted in its case, and on terms which would have its debt paid in full. But unless and until that remedy is granted, the applicant has no equitable interest in the trust assets or equity which appears to have priority over those of other creditors of the trustee. The question then is whether the equitable remedy of subrogation would be granted on terms which would advance one otherwise unsecured creditor ahead of the others and to their detriment. The fact that this creditor has applied for the remedy (although at this hearing it did not pursue that relief) whilst other creditors have not so applied, does not indicate some conduct on the part of every other creditor in the nature of, for example, acquiescence or delay, which might disentitle that creditor to the same remedy. If the applicant's right to be subrogated is no greater than that of any other creditor, the relief which it might hope to obtain would have to be limited to ensure that the rights of the other creditors were not prejudiced.

[9] This question of priorities between the creditors of an insolvent trust is discussed by the authors of *Jacobs' Law of Trusts in Australia* as follows:

> "What is the correct order of priority between trust creditors after payment of administration costs? One suggestion is that where the equities are equal the trust creditors be accorded that priority which reflects the order in which the claims arose, on the basis that as each claim arose it brought with it an interest, via subrogation, in the lien of the trustee over the trust assets. Mr Justice McPherson, writing extra-judicially, has suggested

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10 (1996) 1 WLR 328 at 335.

11 (1996) 134 FLR 368 at 372.

> that the claim be ranked pari passu by analogy with the general principle of equity that requires a distribution of company property in a winding-up to proceed on the footing of equality among the creditors of equal degree. It is submitted *first*, that the analogy with company liquidations is a wide one and, in any event, not only corporate but individual trustees may be involved and there may be a shortfall in trust assets where the trustee, in its own right, is quite solvent and neither bankrupt nor in winding-up; *second*, that it is more accurate to see the lien as one which at best attaches only potentially as the liability of the trustee arises, and crystallises only upon proceedings for its enforcement and upon it being clear that there is a balance on the account between trustee and beneficiary in favour of the former; and *third*, that an appropriate analogy is that favoured in cases of competing claims by beneficiaries of different trusts to trace into a mixed fund, and this produces a ranking pari passu."[12]

[10] The applicant's argument would appear to accept that its claim would have no priority according to when its debt was incurred. And there is no evidence as to the timing of its debt compared with others. The notion that some creditors of the trustee would be able to claim ahead of others, according to when their debts arose, seems inconsistent with subrogation being a remedy rather than a right of action. Rather, as I have said, the applicant attributes its supposed priority to its having commenced proceedings to seek that remedy. But there is no basis in principle or authority for that proposition.

[11] The starting point is that some reason should be demonstrated for departing from what Justice McPherson has described as:

> "the general principle of equity that requires a distribution of company property in winding-up to proceed upon a footing of equality amongst all the creditors of equal degree".[13]

In *Spies v The Queen*,[14] Gaudron, McHugh, Gummow and Hayne JJ said:

> "To give some unsecured creditors remedies in insolvency which are denied to others would undermine the basic principle of pari passu participation by creditors."

And as Owen J said in *Custom Credit Corporation Limited v Ravi Nominees Pty Ltd*:

> "The property of an insolvent company is to be applied in satisfaction of liabilities equally, and the courts look askance at mechanisms which seek to reserve specific assets to settle particular liabilities."[15]

[12] In *Octavo Investments Pty Ltd v Knight*, the joint judgment suggested no possibility that the availability of subrogation might

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12 (2006, 7th ed) at [2115] (citations omitted).
13 B H McPherson, The Insolvent Trading Trust' in P D Finn (ed), *Essays in Equity* (1985) 142 at 158.
14 (2000) 201 CLR 603 at 636.
15 (1992) 8 WAR 42 at 54.

lead to different outcomes between creditors of a trust business according to which of them brought proceedings or to any other matter. Their Honours referred to such creditors as a group when saying that they would be subrogated to the beneficial interest enjoyed by the trustee.[16] In *Re Suco Gold Pty Ltd*, King CJ said that in a case where there was a deficiency in the assets of a particular trust, which had been conducted by a trustee company, creditors not otherwise entitled to priority would rank pari passu.[17]

[13] In *Nolan v Collie*,[18] a claimant who had obtained a judgment against a trustee brought further proceedings to establish that trustee's right to indemnification from the trust and its right to be subrogated to the trustee's position. At first instance, it was declared that the claimant was subrogated to the trustee's rights and thereby to its right of indemnity arising in respect of the earlier judgment. The appeal was unanimously dismissed. One of the unsuccessful arguments was that the declaration ought not to have been made, because the trustee was by then in liquidation and its indemnity had become property available to the liquidator for division amongst other creditors so that the declaration was inconsistent with that position by giving the plaintiff some priority.[19] The principal judgment was given by Ormiston JA, with whom Batt and Vincent JJA agreed, who held that the declaration made in favour of this creditor would not give it a priority over other creditors. Ormiston JA said:

> "The order made by Warren J did not impinge on the liquidator's powers, at least as I would understand the order that she made.
>
> There must therefore be some other reason lying at the back of the appellant's contention. It seems that what in particular is relied upon is the assertion made in the authorities that upon subrogation the party subrogated acquires some equitable interest in the relevant assets. That may be so, indeed there is no doubt that the right of indemnification continues to affect the trust property even though there is a new trustee, but the interest recognised is intended merely to preserve the right of the trustee, not to create a priority of the kind frequently given where other charges are imposed except a right to claim priority over the beneficiaries."[20]
>
> If, according to that judgment, a creditor which had obtained final relief in proceedings to enforce its right of subrogation does not thereby enjoy a priority over other creditors of the trustee, it cannot be the case that the mere commencement of such proceedings could have that result. There is no

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16 (1979) 144 CLR 360 at 367, 370 and 371.

17 (1983) 33 SASR 99 at 109.

18 (2003) 7 VR 287.

19 More precisely amongst all creditors of the trustee, rather than only creditors of the trustee from the carrying out of that trust, consistently with a decision of the Full Court of the Supreme Court of Victoria in *Re Enhill Pty Ltd* [1983] 1 VR 561. In *Re Suco Gold Pty Ltd*, *Re Enhill* was not followed where it was held that the assets of a particular trust had to be applied in payment of liabilities incurred as trustee of that trust.

20 [2003] 7 VR 287 at 313.

> proprietary interest which is derived by the commencement of such proceedings. Unless and until some order is made for the application of property held by the trustee specifically in favour of the applicant, it enjoys no priority over other creditors of the company. It is sufficient to say that such an order is not sought at least within this present application for the termination of the DOCA. But I would not have made such an order had it been sought. According to *Re Suco Gold Pty Ltd*, the company's right to indemnity is property the proceeds of which should be divided according to what is now s 556 of the *Corporations Act* 2001 (Cth). In *Jacobs' Law of Trusts in Australia*,[21] that is said to be incorrect because s 556 is said to deal with the application of the assets beneficially owned by the company and available for distribution between "general" creditors, rather than only creditors from the carrying out of the activities of the relevant trust. Accepting that to be so, still I would have refused such an order because the equitable remedy of subrogation should not be used to engineer an unequal outcome between otherwise unsecured creditors of an insolvent trustee and where to advance one creditor's position would disadvantage that of the others."

[24] His Honour accordingly held that the first ground for terminating the DOCA must fail.

[25] Applying the principles so lucidly articulated by McMurdo J to the present case, it is clear that, by instituting the present proceeding, the applicant was seeking the remedy of subrogation. It is equally clear that this remedy had not been granted as at the date the DOCA was executed. As was the case before McMurdo J, the present applicant seems to assume that the equitable remedy of subrogation would be granted in its case, and on terms which would have its judgment debt paid in full. But, to quote McMurdo J again, "Unless and until that remedy is granted, the applicant has no equitable interest in the trust assets or equity which appears to have priority over those of other creditors of the trustee".

[26] It also necessarily follows that, in the absence of an order for subrogation having been made, the applicant was not a "secured creditor" of the first respondent. At highest, it had, at the date of execution of the DOCA, an inchoate right to seek to be subrogated to the trustee's right of indemnity and the lien or charge which the trustee enjoys over trust assets. But the applicant did not have the benefit of that subrogation on the day the present DOCA was executed.

[27] Accordingly, it seems to me that it cannot be said that the applicant was a "secured creditor" within the meaning of that term in s 444D, and accordingly does not have the benefit of the exclusion set out in s 444D(2).

[28] It follows that the applicant was an unsecured creditor when the DOCA was executed and, by application of cl 7.1 of the DOCA, the debt owed by Zen 28 to the applicant as an unsecured creditor was extinguished by law. It also follows that the correlative indemnity which Zen 28 would otherwise have had from the trust assets was also extinguished because that indemnity clearly only exists while the trustee is personally liable for the debt incurred as a trustee.

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[21] (2006, 7th ed) at [2115].

[29] It is unnecessary to deal with the arguments concerning the caveat, because it was withdrawn in July 2009 upon a sale of the land by a receiver and manager appointed by a secured creditor.

[30] Having reached these conclusions, it is, in my view, clear that the claim by the applicant against the first respondent should be dismissed. It is, in those circumstances, unnecessary for me to consider the argument that the applicant was approaching the Court with unclean hands.

Application for the claim against the second respondent to be dismissed

[31] The claim against the second respondent in this proceeding is for:

> "12. A declaration that the second respondent is indebted to the applicant in the amount of:
>
> (a) $504,411.82 together with interest pursuant to s 47(1) *Supreme Court Act* 1995 (Qld) (or alternatively pursuant to s 67P of the *Queensland Building Services Authority Act* 1991 (Qld) ("QBSA") at the rate of 16.43% per annum) upon the whole of such amount from 5 September 2008 until the date of judgment or earlier payment.
>
> (b) The cost as assessed (or otherwise agreed upon) as payable by the first respondent in the Supreme Court Proceedings 8782/08 at Brisbane by virtue of the order made on 12 September 2008."

[32] The claim is against the second respondent, who was the sole director of Zen 28 and the primary beneficiary under the Zen 28 Trust. The Trust Deed established what is commonly known as a discretionary trust by which the trustee had a wide discretion in relation to, inter alia, the application of trust income for one or more of the primary, secondary and tertiary beneficiaries nominated in the relevant schedule to the Trust Deed. Whilst the second respondent is nominated as the primary beneficiary, the secondary and tertiary beneficiaries nominated in the schedule to the Trust Deed encompass a wide range of relations of the primary beneficiary and further trusts, partnerships and companies in which the primary beneficiary has or in the future may have an interest.

[33] The applicant contends that he has a right to pursue the second respondent by reason of the entitlement which Zen 28 had to claim indemnity from the second respondent who was, as already noted, the sole director of the corporate trustee and thereby, effectively, the controlling mind of the corporate trustee while also being the primary beneficiary under the trust. The first link in this chain is the assertion that Zen 28 had a right to be indemnified by the beneficiaries of the trust for liabilities properly incurred in the trust. When discussing this alternative right which a trustee has to be indemnified by the beneficiaries, McPherson JA in *Ron Kingham Real Estate Pty Ltd v Edgar*[22] said at 442:

> "That right to personal indemnity from a beneficiary has been recognised in various authorities including, most prominently, the decision of the Privy Council in *Hardoon v. Belilios* [1901] A.C. 118, 125, where it was said the

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22 [1999] 2 Qd R 439.

> obligation of a beneficiary to indemnify the trustee rests on "the plainest principles of justice", which require "that the cestui que trust who gets all benefit of the property should bear its burden". See also *Trautwein v. Richardson* [1946] A.L.R. 129, 134-135; and *Marginson v. Ian Potter & Co.* (1976) 136 C.L.R. 161, 175-176, where Jacobs J. quoted with approval a passage from *Halsbury's Laws of England*, 3rd ed., vol. 38, at 943-944, describing the trustee as having the right to an indemnity "from a person sui juris who is beneficially entitled" to the trust property. The right of a trustee to indemnity from the beneficiary is capable of being expressly excluded; but the terms of the trust instrument are not in evidence, and there is nothing at all to suggest that the indemnity was excluded in the case of this Trust.""

[34] Unlike the case which was being considered by McPherson JA, the Trust Deed relating to the present trust is in evidence before me. In relation to the trustee's right to indemnity, cl 7.6 of the Trust Deed provided, inter alia, as follows:

> "7.6 The Trustee and every former Trustee and every director and former director of the Trustee or a former Trustee has (as the case requires) a charge or lien or right of compensation, reimbursement, contribution or indemnity out of an asset or assets of the Trust Fund ("the right") in the following circumstances and in no other:
>
> (a) the liability in respect of which the right is claimed:
>
> (i) did not arise from a breach of trust or duty in which the Trustee or former Trustee or director or former director:
>
> A. failed to act honestly in a matter concerning the Trust fund; or
> B. intentionally or recklessly failed to exercise in relation to a matter affecting the Trust Fund, the degree of care and diligence that a trustee or director is required to exercise; and
>
> (ii) is not a liability for a monetary penalty; and
>
> (b) any one of the following persons determines that the Trustee or former Trustee or director of former director is to have the right, that is to say:
>
> (i) the Trustee (other than a trustee who, if an individual is or becomes bankrupt or enters into or otherwise becomes subject to an arrangement with creditors without sequestration under the *Bankruptcy Act 1966*, or if a company, is or becomes subject to external administration under the *Corporations Act, 2001* or is dissolved), or if either an individual or a company is or becomes insolvent, or has proceedings brought against it, or an order made against it under the *Family Law Act 1975* in its capacity as Trustee (other than for the sole purpose of determining the validity of the trust or the rights or entitlements of the beneficiaries); or
>
> (ii) any director of the Trustee or a former Trustee (other than a director or former director who is or becomes

> insolvent, and other than a director or former director claiming the right of making a similar claim); or
>
> (iii) the Principal; and
>
> (c) unless a person referred to in 7.6(a) decides otherwise:
>
> (i) the property in respect of which the right is claimed is in the Trustee's or former Trustee's actual possession at the time the claim is made; and
>
> (ii) the property in respect of which the right is claimed was in the possession of the Trustee or former Trustee at all times during the period when the events giving rise to the claim occurred.
>
> (d) Except as provided above and in clause 7.6(e), a Trustee or former Trustee or director or former director of a Trustee or former Trustee does not have any right of compensation, contribution, indemnity or other claim against the Trust Fund or any Beneficiary or any other person, because of the Trustee of former Trustee having accepted the office of Trustee or incurred any liability for the benefit of or at the request express or implied of that Beneficiary or other person or otherwise.
>
> (e) The trustee may give such financial assistance as it deems appropriate to any director or other officer for or in connection with advice and/or proceedings concerning any actions or omissions of that officer in relation to the affairs of the trust.
>
> (f) All persons claiming any beneficial interest in over or on the property subject to this Trust shall be deemed to take with notice of and subject to the protection conferred on the Trustee by this Deed.
>
> Without limiting the Trustee's right of indemnity if the Trustee shall in any year make a loss in carrying on any business under this Deed that loss shall not be met out of corpus but shall be carried forward and met out of the income of future years."

[35] There is no evidence before me to suggest that the express exclusion of the trustee's right of indemnity against any beneficiary in cl 7.6(d) is not operative in the present case.

[36] Even if the trustee's right to seek indemnity from the beneficiaries were not excluded in the present case, that would not be the end of the matter. In the *Ron Kingham* case, at 443, McPherson JA referred to the dearth of authority for the proposition that there is a right on the part of a creditor to subrogation to a trustee's claim to indemnity against a beneficiary in person, but went on to say that he could not see that it made any difference in principle whether the creditor claimed to be subrogated to the trustee's right of indemnity against the trust property or against the beneficiary in person. As with the claim brought against the first respondent, the claim against the second respondent is a claim for the remedy of subrogation, by which the applicant seeks to be subrogated to such rights as the trustee has to be indemnified by the second respondent as beneficiary. The intervening DOCA,

however, has operated to extinguish the judgment debt owed by the trustee to the applicant, and it must accordingly follow that:

(a) there is no liability now existing in respect of which the trustee could seek indemnity from the second respondent as beneficiary, and

(b) there is no right of indemnification which could be the subject of the remedy of subrogation. The claim in that regard against the second respondent has therefore been rendered nugatory by reason of the operation of the DOCA.

[37] In all those circumstances, the claim against the second respondent should also be dismissed.

Application by the second respondent concerning the undertaking given on 3 February 2009

[38] By a further interlocutory application, the second respondent has applied for the following orders:

> "1. A declaration that upon its proper construction, the undertaking set out in the consent order issued by this honourable Court and pronounced by his Honour Justice Daubney on 3 February 2009 does not oblige the second respondent to provide a bank guarantee from the National Australia Bank in the amount of $377,635.96;
>
> 2. In the alternative to order 1, the undertaking of the second respondent in the consent order issued by this honourable Court and pronounced by his Honour Justice Daubney on 3 February 2009 to provide a bank guarantee from the National Australia Bank Ltd in the amount of $377,635.96 be discharged."

[39] The terms of the consent order in which that undertaking was given are set out above in paragraph [5]. By reason of several matters, the points sought to be agitated on behalf of the second respondent in this application concerning the undertaking are somewhat moot – the bank guarantee was not provided by the date specified, and the applicant's undertaking to provide a withdrawal of the caveat upon delivery of such bank guarantee was therefore never activated. As noted above, the caveat was ultimately withdrawn upon a sale of the property on behalf of a secured creditor. Moreover, for the reasons I have given above, the claims made in the principal proceeding against the first and second respondents are to be dismissed. As was properly conceded by counsel for the applicant in the course of argument, success by the respondents in their application for summary judgment would be reason enough for discharge of the undertaking. The applicant has not moved to have the second respondent dealt with for contempt for non-compliance with the undertaking. Nor does the applicant point to any prejudice he would suffer if the undertaking were now discharged.

[40] Lest my decision to dismiss the claims against the first and second respondents be considered mistaken, however, it is appropriate that I deal with this application in some further detail.

[41] The second respondent's initial submission was that the undertaking, properly construed, was not given by the second respondent personally, but was given in his

capacity as a director of the first respondent because it incurred the debt, and was an undertaking that he would cause the company to procure the specified guarantee. I would reject that construction, because that is simply not what the undertaking says. On its face, the undertaking was one which was clearly given by both the first respondent and the second respondent, and the action which the first and second respondents undertook to take was "to provide a bank guarantee ... by 10 February 2009". The second respondent, on the face of the undertaking, was certainly bound by its terms.

[42] The more substantial point, however, is the second respondent's argument that, to the extent that this undertaking bound him personally, he did not give instructions to his solicitor to give this undertaking on his behalf.

[43] Affidavits by both the second respondent and his solicitor were filed and read, and both of them were cross-examined before me. The second respondent's evidence was that when the matter was before the Court on 4 November 2008, the second respondent was not present in Court. He had a telephone discussion with his solicitor, during which the solicitor told him that he was in discussions with the other parties and a proposal for consent orders was to be provided. About an hour later his solicitor phoned him and said that agreement as to the form of orders had by and large been reached but there were some final issues to be sorted out. The second respondent was not shown a copy of the proposed consent orders at that time. Between November 2008 and January 2009, he heard nothing more about the terms of the orders and, when he spoke with his solicitor over that time, his solicitor indicated that he had not heard any further from the applicant's solicitor. On 2 February 2009, his solicitor told him that the matter was listed for 10 February and that the lawyers were finalising the consent orders to be presented to the Court on that day. His solicitor told him that the solicitor would be conferring with the other parties on the afternoon of 2 February. He had a further telephone discussion with his solicitor when he was informed that the solicitor was about to go onto a conference call to discuss the matter with the relevant parties. The second respondent deposed:

> "At all times, I believed there was a requirement for the company to provide a guarantee, but was not aware that there was any suggestion that I would be asked to provide a bank guarantee.
>
> Instead, I understood that the proposed orders related solely to Zen 28 Pty Ltd providing the undertaking and Mr Nickless would, with the other parties, agree on the final wording of the orders which would be presented at the appearance on 10 February. At no time did I ever authorise Mr Nickless or anyone to consent to orders that I provide a bank guarantee.
>
> On 2 February 2009 Mr Nickless sent me a further email with communication between Mills Oakley, Freehills and Hynes Lawyers, providing a copy of the draft orders. Again, I did not open or look at the orders as I understood that they were only drafts and did not contemplate in any way that they would arguably impose an obligation upon me to personally obtain a bank guarantee."

The second respondent exhibits to his affidavit an email from his solicitor with which was enclosed a copy of the draft order, including the terms of the

undertakings, in terms identical to that made by me on 3 February 2009, but says that he did not read this at the time.

[44] The second respondent says that on 5 February 2008 he was told by a bank officer that the consent orders required the second respondent to personally provide a bank guarantee. After that phone conversation, the second respondent telephoned his solicitor, and was told for the first time that the consent orders required him to provide a bank guarantee. The second respondent said that he was "shocked and furious that such consent orders could be signed without my full understanding of the matter". He said that he did not see a copy of the signed orders until 9 February 2009.

[45] No real inroads were made into the second respondent's credit in respect of this evidence when cross-examined, and indeed he reaffirmed on several occasions the fact that he was ignorant of an undertaking having been given on his behalf personally until he was notified of that by the bank.

[46] The second respondent's then solicitor also swore several affidavits, and was cross-examined before me. In relation to the form of consent order, he confirmed that he did not advise the second respondent that an undertaking in that form could impose a personal liability on the second respondent. He said:

> "I did not appreciate at the time of executing [the consent order] that the undertaking could be read as requiring Mr Lee to provide the bank guarantee referred to in the undertaking set out therein. I certainly did not advise Mr Lee of this because I did not appreciate it myself and in fact, the whole dispute had been focused upon the disputed liability of Zen 28 and Zen 28 providing a bank guarantee."

[47] The solicitor gave further evidence which was completely consistent with the second respondent's version when he deposed to the following:

> "On 5 February 2009 I received a telephone call from George Lee. Mr Lee told me that he had spoken to someone from the Bank and they told him that he was personally required to provide a bank guarantee. He told me that he was very upset and indicated to me that he had never agreed to personally providing a bank guarantee. That was consistent with my understanding in that Mr Lee had never instructed that he was prepared to execute any or undertake to the Court or otherwise that he would personally give a bank guarantee.
>
> It was never my intention that the orders contain any undertaking by Mr Lee to provide a bank guarantee. It was not until that telephone call with Mr Lee that I appreciated the orders could arguably contain a requirement that Mr Lee provide a guarantee."

[48] The solicitor expanded on this explanation in a further affidavit, in which he deposed to the following:

> "4. As I swore in my first affidavit, I did not appreciate when I signed the consent order on 2 February 2009 that the undertaking might be construed as an undertaking by Mr Lee personally.

5. On 5 February 2009, I had a telephone conversation with Mr Lee. I cannot now recall whether he telephoned me or I telephone him. We had a telephone conversation to the following effect:

   Mr Lee: "*James, what the hell is going on? Justin [Ottway, from Mr Lee's bank] just told me that the orders require a bank guarantee to be provided by me. Me, personally, not just Zen 28.*"

   Me: Silence [I was surprised and began to flick through the file to try to find the consent order].

   Mr Lee: "*James! Is that right?*"

   Me: Silence [I had not yet located the consent orders].

   Mr Lee: "*That had better not be the case.*"

   Me: "*The undertaking is on behalf of Zen 28 and you personally.*"

   Mr Lee: "*What! How could that even happen? I never said that I would personally give a bank guarantee! What have you done?*"

   Me: "*I don't know George, I must have missed it. I've stuffed up.*"

   Mr Lee: "*Well, you better fix it.*"

6. The email from Mr Lee to Mr Higginson which became exhibit 1 on the hearing before the Honourable Justice Daubney on 5 October 2009 was sent by Mr Lee very shortly after the conclusion of our telephone conversation.

7. Until that telephone conversation with Mr Lee, I have not thought that the consent order might be understood as containing an undertaking by Mr Lee personally to provide the bank guarantee. I did not have instructions from Mr Lee to offer a personal undertaking on his behalf. When I looked at the consent order during my telephone conversation with Mr Lee on 5 February 2009, I appreciated for the first time that the undertaking may be construed as having been given by Mr Lee personally.

8. I was admitted as a legal practitioner of this Honourable Court in March 2007. I understand that giving an undertaking to the court on behalf of a client is a serious matter and requires the client's specific instructions.

9. If this Honourable Court concludes that the consent order of 3 February 2009 contains an undertaking by Mr Lee personally to provide the bank guarantee, I humbly apologise to Mr Lee for signing the consent order having that effect without his specific instructions. I also humbly apologise to this Honourable Court. I made a mistake in not reading the consent order carefully enough and not appreciating that it might be construed in that way. I did not intend to mislead the court or Mr Adams, to whom I also humbly apologise for my mistake."

[49] Again the credit and credit-worthiness of these matters deposed to by the solicitor were not shaken under cross-examination.

[50] In short, on the evidence before me, it appears clear that the solicitor did not have instructions to give an undertaking on 3 February 2009 in terms which bound the second respondent personally. That such an undertaking was given is beyond doubt – a form of consent order signed by the solicitors for each party was tendered to me and placed on the file. There is also no doubt that the solicitor had ostensible authority to give that undertaking on behalf of the second respondent. The solicitor did not, however, have actual authority to give that undertaking. Nor, in my view, could it properly be said that a solicitor has implied actual authority, by reason of a retainer for a client in litigious matters, to give undertakings to the Court. On the contrary, given the gravity of the fact and act of giving an undertaking to the Court and the potential for very serious adverse consequences to flow in the event of a breach of an undertaking, it is, in my view, clear that a legal practitioner giving an undertaking to the Court on behalf of a client ought have specific instructions on the specific terms of the specific undertaking.

[51] This is not an application for the second respondent to be punished for non-compliance with the undertaking given to the Court. It is therefore unnecessary for me to consider what, if any, consequences might have flowed for him from the fact that the solicitor gave the undertaking on his behalf without instructions.

[52] Given the absence of any prejudice to the applicant, and the clear position on the evidence that the undertaking was given on behalf of the second respondent without specific instructions from the second respondent to give a personal undertaking on his behalf, I am satisfied that this is an appropriate case in which, to the extent that it remains necessary, the second respondent ought henceforth be discharged from the undertaking given to the Court on 3 February 2009.

Conclusion

[53] On the application for summary judgment, there will be orders that the claims against the first respondent and the second respondent be dismissed.

[54] On the second respondent's application concerning the undertaking, there will be an order that the undertaking of the second respondent in the order pronounced by me on 3 February 2009 to provide a bank guarantee from the National Australia Bank Ltd in the amount of $377,635.96 be henceforth discharged.

[55] I will hear the parties as to costs in respect of these applications.