

SUPREME COURT OF QUEENSLAND

CITATION: *In the matter of First Strategic Development Corporation limited (in liquidation) v Jonathan Paul McLeod as liquidator of First Strategic Development Corporation limited (in liquidation)* [2011] QSC 143

PARTIES: **IN THE MATTER OF FIRST STRATEGIC DEVELOPMENT CORPORATION LIMITED (IN LIQUIDATION) ACN 128 309 651**

JONATHAN PAUL McLEOD AS LIQUIDATOR OF FIRST STRATEGIC DEVELOPMENT CORPORATION LIMITED (IN LIQUIDATION) ACN 128 309 651
(Applicant)

FILE NO/S: BS 1821 of 2011

DIVISION: Trial Division

PROCEEDING: Application for directions

ORIGINATING COURT: Supreme Court of Queensland

DELIVERED ON: 1 June 2011

DELIVERED AT: Brisbane

HEARING DATE: 20 May 2011

JUDGE: Boddice J

ORDER: **The application is approved**

CATCHWORDS: CORPORATIONS – WINDING UP – LIQUIDATORS – RIGHTS AND POWERS – IN WINDING UP BY COURT – PROCEEDINGS BY LIQUIDATOR – where liquidator seeks an order pursuant to s 477(2B) of the *Corporations Act* 2001 (Cth) – where liquidator has entered into funding agreement with a creditor to fund a public examination and possible recovery proceedings – where various considerations relevant to exercise of Court’s discretion – whether the funding agreement ought to be given retrospective approval

Corporations Act 2001 (Cth)

Corporate Affairs Commission v ASC Timber Pty Ltd (1998)
29 ACSR 109

Re ACN 076 673 875 Ltd (2002) 42 ACSR 296

Re Imobridge Pty Ltd (in liq) (No 2) [2000] 2 Qd R 280

Stewart, in the matter of Newtronics Pty Ltd [2007] FCA
1375

COUNSEL: Martin, M for the applicant

Jennings, C for the respondent

Atkinson, D for the third party

SOLICITORS: Shand Taylor Lawyers for the applicant

- [1] Jonathan Paul McLeod (“McLeod”), the liquidator of First Strategic Development Corporation Limited (in liquidation) (“the Company”), seeks an order pursuant to s 477(2B) of the *Corporations Act 2001 (Cth)* (“the Act”) approving a funding agreement he has entered into with a creditor, Macarthur Minerals Limited (“Macarthur”) to fund a public examination and possible recovery proceedings.
- [2] McLeod’s application is supported by Macarthur (which was given leave to appear) and by other creditors of the Company.¹ It is opposed by two creditors of the Company, Wai Tak Kwok (“Kwok”) and Australia China Metal Corporations Pty Ltd (“ACMC”) (who were given leave to appear) on the basis:
- (a) approval has not been sought from the creditors of the Company;
 - (b) the funding agreement is not reasonable; and
 - (c) there is a conflict of interest.

Background

- [3] The Company, which was incorporated on 28 March 2008, operated as a mining exploration and management company. It employed no staff other than its directors. In December 2009, it acquired an option to purchase a mining tenement in Western Australia. The option period was 12 months and required the Company to expend approximately \$2.5 million in exploration costs.
- [4] At or around the time of the acquisition of that option to purchase, the Company appointed new directors, including Kwok. The former directors resigned, including Alan Spence Phillips (“Phillips”) and David Charles Eton Taplin (“Taplin”).

¹ Affidavit of John Saunders, pp.s 23 – 32

- [5] Between December 2009 and November 2010, the Company incurred substantial debts. During this time, discussions were had between the directors of the Company and Macarthur with respect to the acquisition of shares in the Company. No such acquisition took place.
- [6] On 17 November 2010, the Company was wound up pursuant to s 491(1) of the Act. Initially, David Ross and Richard Albarran were appointed liquidators of the Company. However, on 14 February 2011, Ross and Albarran were removed as liquidators and replaced by McLeod.
- [7] Ross and Albarran provided a report to creditors dated 19 November 2010. It advised the Company had liabilities of \$1,894,405.98, and assets of \$269.54. Almost half of the liabilities relate to claims by directors or other entities in which directors have an interest. There are also many unrelated creditors. Macarthur is a creditor of the Company.
- [8] McLeod has obtained orders for the examination of the directors of the Company appointed on or after 25 November 2009, including Kwok. The purpose of the examination is to ascertain whether a claim for insolvent trading should be prosecuted. All of the sums claimed by creditors were incurred after December 2009. The examination is listed to take place in the Magistrates Court, Brisbane on 3 and 9 June 2011.

Funding agreement

- [9] The funding agreement, between McLeod, the Company and Macarthur, provides that Macarthur will fund the costs and expenses of conducting the public examinations and obtaining advice from Senior Counsel as to whether any proceedings ought to be commenced and prosecuted in respect of recovery action for the benefit of creditors of the Company, including any appeals.
- [10] Relevantly, the funding agreement contained the following terms:
- “1.5 “Lawyers” means Shand Taylor Lawyers and Counsel retained by them.
- 1.7 “Legal Costs and Disbursements” means the legal costs and disbursements reasonably incurred by McLeod with the Lawyers for the sole purpose of conducting the Public Examinations and obtaining Senior Counsel’s advice as to the prosecution of the Proceedings on behalf of McLeod and/or FSDC.
- 1.9 “Public Examinations” means the examination of the officers of FSDC and any other person who may be able to provide information about FSDC’s examinable affairs.”
- ...
4. The Lawyers’ Retainer and Instructions
- 4.1 The lawyers are instructed by McLeod not by Macarthur. However, the Legal Costs and Disbursements will be paid solely by Macarthur.

- 4.2 Macarthur will not interfere with the conduct of the Public Examinations or the Proceedings. However, McLeod will report regularly to Macarthur on the progress on the Public Examinations and the Proceedings and undertakes to take into account any comments, suggestions or observations made by Macarthur about McLeod's conduct of the Public Examinations and the Proceedings.
- 4.3 McLeod acknowledges that representatives of Macarthur may have, from time to time, relevant information and/or documentation which may assist the Lawyers with the Public Examinations and the Proceedings, and that those representatives of Macarthur may, from time to time, have direct contact with the Lawyers for the purposes of passing on that information and/or that documentation.
- 4.4 If McLeod wants to settle the Proceedings, McLeod will advise Macarthur of the proposed terms of settlement, and if Macarthur disagrees with the terms upon which McLeod intends to settle the proceedings, then McLeod will give Macarthur a reasonable opportunity to make submissions. However, if McLeod and Macarthur are unable to resolve their differences, McLeod retains the unfettered power to conduct and settle the proceedings.

...

7. Funding Costs and Commission

- 7.1 Upon Resolution, and before any other payments are made from the Resolution Sum, McLeod and FSDC will pay to Macarthur from the Resolution Sum:
- a) An amount equal to the total of all Funding Costs paid by Macarthur to such time; and
 - b) An amount equal to 10% of the Resolution Sum.”

Law

- [11] Section 477(2B) of the Act provides that except with the approval of the Court, of the committee of inspection or of a resolution of the creditors, a liquidator of a company must not enter into an agreement on the company's behalf. A Court has a discretion to grant approval. Approval may be given retrospectively.²

² *Stewart, in the matter of Re Newtronics Pty Ltd* [2007] FCA 1375 at [25].

[12] The principles relevant to the exercise of the power were not in dispute. A key consideration is whether the liquidator believes it will be for the benefit of the company and its creditors.³ Factors to be considered include:⁴

- (a) the nature and complexity of the cause of action;
- (b) the amount of costs likely to be incurred in the conduct of the action and the extent to which the financier is to contribute to those costs;
- (c) the extent to which the financier is to contribute towards the costs of the defendant in the event that the action is not successful, or towards any order for security for costs by the court before which the action is to be heard;
- (d) the extent to which the liquidator has canvassed other funding options;
- (e) the level of the financier's "premium";
- (f) the risks involved in the claim; and
- (g) the liquidator's consultations with the creditors of the company.

[13] In exercising the discretion, the task of the Court is:

“[not] to reconsider all of the issues which have been weighed up by the liquidator in developing the proposal, and to substitute its determination for his in....a hearing de novo [but]... simply to review the liquidator's proposal, paying due regard to his or her commercial judgment and knowledge of all of the circumstances of the liquidation, satisfying itself there is no error of law or ground for suspecting bad faith or impropriety, and weighing up whether there is any good reason to intervene in terms of the 'expeditious and beneficial administration' of the winding up.”⁵

[14] Where it is alleged that a funding agreement is attended by bad faith, it is insufficient to merely show that the liquidator or the solicitors will secure some advantage, especially where the evidence suggests the arrangements overall will benefit creditors.⁶ There is a public interest in bringing directors to account and ensuring that creditors can pursue potential claims.⁷

³ *Re ACN 076 673 875 Ltd* (2002) 42 ACSR 296 at [16] – [17], [36]

⁴ *Re ACN 076 673 875 Ltd* (2002) 42 ACSR 296 at [28]

⁵ *Corporate Affairs Commission v ASC Timber* (1998) 29 ACSR 109 at pp. 118; *Stewart, in the matter of Re Newtronics Pty Ltd* [2007] FCA 1375 at [26] .

⁶ *Re ACN 076 673 875 Ltd* (2002) 42 ACSR 296; *Re Imobridge Pty Ltd (in liq0 (No 2))* [200] 2 Qd R 280.

⁷ *Re ACN 076 673 875 Ltd* (2002) 42 ACSR 296 at [39]

The application

- [15] Kwok and ACMC rely on the following matters to support their opposition to approval of the funding agreement:
- (a) Kwok is a director and beneficial shareholder in companies which are substantial shareholders in Macarthur. One of those companies brought proceedings for inspection of records of Macarthur pursuant to s 247A of the Act.
 - (b) Macarthur, by its directors Phillips and Taplin and its project manager Joe Phillips, sold the Company to Kwok and the other directors on certain arrangements. Kwok and the other directors allege that Macarthur, as part of those arrangements, agreed to buy the Company and made representations in relation to the value of the Company at the end of the exploration phase.
 - (c) Kwok raised these matters with the former liquidators, who indicated further investigations were required as the breakdown in negotiations between the Company and Macarthur contributed to the liquidation of the Company.
 - (d) McLeod was appointed as liquidator of the Company when the former liquidators, appointed by Kwok and a fellow director, Charles Chan, were removed pursuant to an application by Macarthur and other creditors of the Company.
 - (e) There is considerable animosity between Kwok and Phillips and his son.
 - (f) McLeod does not intend to publicly examine Phillips and another former director, Phillips's daughter, because they are "cooperating".
 - (g) Shand Taylor, who are appointed as McLeod's lawyers under the funding agreement, have previously acted in a matter in which they received instructions directly from Phillips. Shand Taylor have also previously represented Phillips and his wife in litigation, and Macarthur and Phillips in other litigation.
- [16] Kwok and ACMC contend that the terms of the funding agreement, when viewed against these circumstances, will produce benefits to Shand Taylor and Macarthur without there being any evidence about the extent to which the funding agreement may ultimately derive any benefit for the creditors of the Company generally. Further, there is a clear conflict of interest as McLeod is required to engage, as solicitors, a firm previously used by Phillips and Macarthur when there is the potential for the conduct of Phillips and/or Macarthur being the subject of further enquiry. McLeod should have access to independent legal advice.
- [17] At the hearing, McLeod, supported by Macarthur, contended for approval of an amended funding agreement which allowed McLeod to appoint solicitors other than Shand Taylor Lawyers and deleted a requirement that McLeod take into account any comments, suggestions or observations made by Macarthur about McLeod's conduct of the public examinations and the proceedings. Kwok and ACMC contend the proposed amended funding agreement still fails to address the clear conflict that arises from Shand Taylor continuing to act on behalf of McLeod.

Findings

- [18] Whether the amended funding agreement ought to be approved requires a consideration of its terms, having regard to all of the surrounding circumstances, including the allegations of conflict of interest.
- [19] In exercising my discretion whether to approve the amended funding agreement, the following factors are relevant:
- (a) The debts incurred by the Company were incurred over a relatively short period of approximately 12 months during which time the Company had no visible means of income. Against that background, any litigation is likely to be confined in terms of the time period in question.
 - (b) The costs involved are likely to be limited when viewed proportionally against the potential sums that could be recovered.
 - (c) Macarthur offers an indemnity for any adverse costs order.
 - (d) If the funding agreement is not approved, Mr McLeod has no funds available to him to conduct the public examination.
 - (e) The public examinations, and funding thereof, are supported by the majority of creditors of the Company. Whilst they are opposed by Kwok and his related entity, this opposition must be viewed in the context that Kwok is one of the directors the subject of the public examination. Consultations with the creditors of the Company are of particular importance in applications of this type.⁸
 - (f) The payment of 10% of the resolution sum is not exorbitant when viewed against similar funding arrangements.⁹ Whilst Kwok and ACMC submit the resolution sum may be obtained without proceedings being instituted, and could result in a windfall to Macarthur, it is likely substantial negotiations would be involved before any resolution. Those negotiations would be conducted by McLeod and funded by Macarthur. Against that background, a 10% premium is reasonable and does not amount to a “windfall”.
 - (g) Whilst the proposed public examination presently involves the examination of Kwok and his fellow directors, and does not involve the examination of Phillips and Taplin, the funding agreement does not restrict the public examination only to officers of the Company. It expressly provides that public examination means “any other person who may be able to provide information about FSDC’s examinable affairs”.¹⁰
 - (h) The amended funding agreement does not require McLeod to only obtain advice from Shand Taylor Lawyers. McLeod may appoint such other solicitor or solicitors from time to time and any counsel retained by them.
 - (i) The amended agreement does not require McLeod to take into account any comment, suggestions or observations made by Macarthur about this

⁸ *Re Imobridge Pty Ltd (in liq) (No 2)* [2000] 2 Qd R 280 at 297.

⁹ Affidavit of McLeod, para 10-12

¹⁰ Exhibit 2 at para 1.9

conduct. Whilst it provides that McLeod will report regularly to Macarthur on the progress of the public examinations and the proceedings, this is an unsurprising requirement having regard to the fact that Macarthur is funding the proceedings and the specific acknowledgement that Macarthur may have relevant information and documentation which will be of assistance to McLeod in the public examinations. Importantly, it occurs in circumstances where McLeod expressly retains an unfettered power to conduct and settle any proceedings that may be brought in respect of the Company's affairs.

- (j) There is no reasonable basis to challenge the impartiality of McLeod, and the amended funding agreement gives him a discretion as to the persons to be the subject of the public examination and as to the solicitors from whom he may seek advice from time to time. Against that background, there is no proper basis to suspect bad faith or impropriety and no good reason to intervene in his administration of the winding up of the Company.
- (k) There is no reasonable basis to find Shand Taylor Lawyers will not act professionally and in accord with their ethical obligations. Should a conflict arise, McLeod can appoint other solicitors.
- (l) Any summonses issued seeking the public examination of a witness can only be issued by order of the court. There is power for any proposed examinee to take steps to set aside that summons for abuse of process.

[20] Having considered all of the material, I am satisfied, in the exercise of my discretion, that it is appropriate to approve the amended funding agreement.¹¹ That amended funding agreement ensures McLeod has access to independent advice.¹² It provides funding for the public examination and for advice from senior counsel in relation to the bringing of proceedings for recovery of debts. That ultimately is beneficial to the winding up as a whole, and creditors in general. Without this funding agreement, no public examination is reasonably likely to occur, with the result that the prospect of proceedings being brought would be significantly impaired.

Conclusions

- [21] I am satisfied the amended funding agreement, in the form of exhibit 2, should be approved pursuant to s 477(2B) of the Act.
- [22] I shall hear the parties as to costs.

¹¹ Exhibit 2.

¹² *Re Imobridge Pty Ltd (in liq) (No 2)* [2000] 2 Qd R 280 at 299 [46].