IN THE COURT OF APPEAL

[1993] QCA 416

SUPREME COURT OF QUEENSLAND

Appeal No. 75 of 1993

Before The President
Mr Justice Pincus
Mr Justice Moynihan

[Starkey v. APA Transport Pty. Ltd.]

BETWEEN:

GRAHAM LINDSAY STARKEY in his capacity as Liquidator of ALLAN FITZGERALD PTY. LTD. (IN LIQUIDATION) Appellant

- and -

APA TRANSPORT PTY. LTD.

Respondent

REASONS FOR JUDGMENT - THE PRESIDENT

Judgment delivered 20/10/93

This is an appeal and cross-appeal from orders made in the Trial Division on 30 March 1993 in the course of the winding up of an insolvent company, Allan Fitzgerald Pty. Ltd. (in liquidation) (the "company"). There were two applications before the Court, one by the liquidator of the company, Graham Lindsay Starkey (the "liquidator"), to which a creditor of the company, APA Transport Pty. Ltd. ("APA"), was respondent, and the other by APA to which the liquidator was respondent. Both applications related to payments made by the company to APA. The liquidator sought to have it determined that (i) two payments made on 28 November 1986 had the effect that APA received a "preference , priority or advantage over other creditors" of the company which was void under section 451 of the Companies (Queensland) Code and (ii) two later payments were void under section 368 of the Code. APA sought to validate the two later

payments under the latter section. Both applications were made after an order had been made for the winding-up of the company. The first two payments which the liquidator sought to impugn were made during the period of 6 months before the filing of the winding up application. The other two payments, which the liquidator sought to have declared void and APA sought to have validated, were made in the period between the filing of the winding up application and the making of the winding up order.

Because there is a dispute concerning the relationship between sections 451 and 368 of the Code, it is desirable first to set out those sections and subsection 365(2) of the Code. As is common ground, the operation of section 451 involves consideration of section 122 of the Bankruptcy Act 1966 (Commonwealth), which is also set out below in so far as it is material.

(i) Companies Code:

"**365(2)** ... the winding up shall be deemed to have commenced at the time of the filing of the application for the winding up.

...

Avoidance of dispositions of property, attachments, &c.

368(1) Any disposition of property of the company, ... after the commencement of the winding up by the Court is, unless the court otherwise orders, void.

...

368(2) Notwithstanding sub-section (1), the Court may, where an application for winding up has been filed but a winding up order has not been made, by order -

(a) validate the making, after the filing of the application, of a disposition of property of the company; ...

on such terms as it thinks fit. ...

...

Undue preference

451(1) ... a payment made ... by a company that, if it had been made or incurred by a natural person, would, in the event of his becoming a bankrupt, be void as against the trustee in the bankruptcy, is, in the event of the company being wound up, void as against the liquidator.

451 (2) For the purposes of sub-section (1), the date that

corresponds with the date of presentation of the petition in bankruptcy in the case of a natural person is -

(a) in the case of a winding up by the Court -

...

(iii)... - the date of the filing of the application for the winding up; ...

451(3) For the purposes of this section, the date that corresponds with the date on which a person becomes a bankrupt is the date on which the winding up of the company commences or is deemed to have commenced.

...

(ii) Bankruptcy Act

"Avoidance of preferences

122. (1) ... a payment made, ... by a person who is unable to pay his debts as they become due from his own money (in this section referred to as **"the debtor"**), in favour of a creditor, having the effect of giving that creditor a preference, priority or advantage over other creditors, being ... a payment ... made ... .

(a) within 6 months before the presentation of a petition on which, or by virtue of the presentation of which, the debtor becomes a bankrupt; or

(b) on or after the day on which the petition on which, or by virtue of presentation of which, the debtor becomes a bankrupt is presented and before the day on which the debtor becomes a bankrupt;

is void as against the trustee in the bankruptcy.

...

(2) Nothing in this section affects -

(a) the rights of a ... payee ... in good faith and for valuable consideration and in the ordinary course of business;

...

(3) The burden of proving the matters referred to in subsection (2) lies upon the person claiming to have the benefit of that subsection.

(4) For the purposes of this section;

...

(c) a creditor shall be deemed not to be a ... payee ... in good faith if the ... payment ... was ... made ... under such circumstances as to lead to the inference that the creditor knew, or had reason to suspect:

(i) that the debtor was unable to pay his debts as they became due from his own money; and

(ii) that the effect of ... payment ... would be to give him a preference, priority or advantage over other creditors.

... ."

Some difficulty occurs (a) in the interaction between (i) subsections (1) and (2) of section 368 of the Code & (ii) sections 368 and 451 of the Code, and (b) in the incorporation in section 451 of the Code of section 122 of the Bankruptcy Act. Between them, sections 368 and 451 of the Code are plainly intended to encompass the entire "preference period", beginning 6 months before the filing of a winding-up application. Further, the two sections must be intended to complement each other, not to impose potentially inconsistent regimes for all or part of that period. When these objectives are met, some overlap between subsections (1) and (2) of section 368 results. 1. It is possible to take section 451 of the Code and to incorporate section 122 of the Bankruptcy Act. Sub-section 451(1), with section 122 of the Bankruptcy Act incorporated in accordance with the dictates of subsections 451(2) and (3) and sub-section 365(2) of the Code, would provide:

> "... a payment made ... by a company that is unable to pay its debts as they become due from its own money (in this section referred to as 'the debtor') in favour of a creditor having the effect of giving that creditor a preference priority or advantage over other creditors, being ... a payment ... made ...
> (a) within 6 months before the date of the filing of the application for the winding up; or
> (b) on or after the day on which the application for winding up is filed and before the day on which the winding up of the company commences or is deemed to have commenced;
> is void against the liquidator."

Because of sub-section 365(2) of the Code, the two dates provided for in sub-section 451(1)(b) coincide, with the result that, where a company is wound up by the Court consequent upon a winding up application being filed, sub-section 451(1)(b) has no material operation. Sub-section 451(1) is, in such circumstances, confined to payments during the period from the date which was 6 months before the filing of the winding up application to the date on which the application was filed.

The liquidator relies upon section 451 as the basis of his

application in relation to the two payments made during the six months before the filing of the winding up application.

2. Subsection 368(2) is concerned with the validation of payments made after the filing of the winding-up application and before the winding-up order is made; an order for validation under subsection 368(2)must be made during that period: (A payment by a company to a creditor is a "disposition of property" within the meaning of section 368: see, eg; Tellsa Furniture Pty. Ltd. (in liquidation) v. Glendave Nominees Pty. Ltd. (1987) 9 NSWLR 254; Re Allan Fitzgerald Pty. Ltd. (in liquidation) [1989] 2 Qd.R. 495; Re Transconsult Australia Pty. Ltd. (in liquidation) (1991) 9 ACLC 1052).

3. Subsection 368(1) permits an order for validation of a payment to be made after a winding up order is made: Tellsa Furniture Pty. Ltd. (in liquidation) v. Glendave Nominees Pty. Ltd.; Bianco Hiring Services Pty. Ltd. v. Adelaide Truss and Frame Pty. Ltd. (in liquidation) (1992) ACSR 609 at 611. The payment validated may have been made (i) after the filing of the winding up application and before the winding up order is made or (ii) after the winding up order is made: Krextile Holdings Pty. Ltd. v. Widdows; Re Brush Fabrics Pty. Ltd. [1974] VR 689 at 696; Ford, H.A.J. Principles of Company Law 5th ed. 1790, 794; contra Sheahan & Anor. v. Workers Rehabilitation and Compensation Corporation (1991) 101 ALR 431 at 445-446. By virtue of subsection 365(2), "the commencement of the winding up by the Court" for the purposes of subsection 368(1) is the time of the filing of the application for winding up:

The liquidator relies upon subsection 368(1) to have the two payments made between the filing of the winding up application and the making of the winding up order declared void, and APA relies upon the same subsection to have those payments validated.

4. While section 451 relates to the earliest material period, the 6 months before a winding-up application is filed, it gives no discretion to the Court to validate payments made in

that period which are not received by the payee in good faith and for valuable consideration and in the ordinary course of business. The section itself makes such payments void even if the material transactions are actually or potentially to the advantage of a company and thus its creditors to be benefited by its winding-up and the division of its assets. For example, if the conditions prescribed by section 451 exist, a vital supplier of goods and services cannot be paid what it is owed in order to secure the provision of more goods or services to permit the insolvent company to continue to trade, even profitably, or so that it might be sold as a going concern.

This position is ameliorated to a degree if the relationship between debtor company and creditor involves a running account. Then, the question whether a payment had the effect of giving the creditor a preference priority or advantage is "to be decided not by considering its immediate effect only but by considering what effect it ultimately produced in fact": Rees v. Bank of N.S.W (1964) 111 CLR 210, 221-222. The liquidator can choose any point of time during the material period as the commencement of the operations on the running account which are said to give a payee a "preference, priority or advantage over other creditors". Rees p.221.

5. Anomalously, after a winding-up application has been filed, and even after a winding-up order has been made, the Court has a wide discretion to validate payments. While a payment made in this period which is received by the payee in good faith and for valuable consideration and in the ordinary course of business (ie., which would not be void under section 451 of the Companies Code if made within the 6 months before the winding-up) will usually be validated under subsection 368 of the Code, that is not the full extent of the Court's discretion under that section. Indeed, the cases emphasise that, because the circumstances may differ widely, it is inappropriate to lay down rigid rules concerning the exercise of that discretion. However, even if the payee does not receive a payment in good

faith and for valuable consideration and in the ordinary course of business, it is ordinarily sufficient if the transaction "offers actual or prospective advantage" to the company and its creditors: Jardio Holdings Pty. Ltd. v. Dorcon Constructions Pty. Ltd. (1984) 3 F.C.R. 311, 316-317. The Court "will take into account whether the payment, and the transaction of which it is part, was or was apt to be for the benefit of the creditors ....": per Mahoney JA. in Tellsa Furniture Pty. Ltd. (in liquidation) p.257. See also Re Allan Fitzgerald Pty. Ltd. (in liquidation).

6. The "running account" principle (see 4 above) was developed in connection with section 122 of the Bankruptcy act and earlier sections to the same or similar effect, all of which relate to the entire period from the date 6 months prior to the bankruptcy petition to the date of the sequestration order. As noted above, for present purposes section 451 of the Code relates only to the period from the date 6 months before the filing of the winding up application to the date the winding up application is filed. It is section 368 of the Code which relates to the subsequent period from the filing of the winding up application up to and following the winding up order.

In these circumstances, a question arises as to whether the "running account" principle operates only during the period covered by section 451 or also for at least part of the period covered by section 368, namely, from the filing of the winding up application to the making of the winding up order.

The "running account" principle is directly concerned with whether or not a payment had the effect of giving the payee a "preference priority or advantage over other creditors", a question which is immediately related only to the operation of section 451, not to its operation in conjunction with section 368. Further, any attempt to combine the operation of the two provisions might produce significant difficulties in practice because of the different approaches which each requires. The different schemes provided for by the different sections would

operate differently in respect of the same payments. One, section 368, but not the other, section 451 involves discretionary considerations. Further, in some cases, including perhaps the present, any attempt to apply the "running account" principle to the total of the separate periods covered by sections 451 and 368 could involve conflict and circuity; for example, a decision to validate a payment under section 368 although not received in good faith and for valuable consideration and in the ordinary course of business might have the effect of increasing the payee's "preference priority or advantage over other creditors" with the possible consequence that the payee does not obtain the full benefit of the validated payment.

The better course seems to be to confine the direct operation of the "running account" principle to circumstances in which section 451 is at issue, and authority generally supports this course. See, for example, Tellsa Furniture Pty. Ltd. at pp.261-262; National Acceptance Corporation v. Benson (1988) 12 NSWLR 213; Re Allan Fitzgerald Pty. Ltd. at pp. 500, 502; Re Transconsult Australia Pty. Ltd.; Sheahan v. Workers' Compensation and Rehabilitation Commission (1991) 9 ACLC 1303; Adelaide Truss and Frame Pty. Ltd. (in liquidation) v. Bianco Hiring Services (1991) 9 ACLC 1348; (1992) 9 ACSR 609.

The facts to which the above principles must be applied can be stated quite briefly.

There was a long-standing business relationship between the company and APA when the first of the impugned payments was made on 28 November 1986. The company conducted the business of an engineering contractor and APA supplied trucks to it for that purpose. APA invoiced the company on a regular basis and, at the end of each month, provided a statement summarising the amounts due. Payment was routinely made within 30 days from the end of the month in which an invoice was sent. Commonly, payment was made to APA by the company from a progress payment received under one of its work contracts, which at relevant times were

very substantial, usually a progress payment which included the work or services performed by APA for which it was being paid.

APA's records included details of its debtors, including the company, during 1986 and to June 1987, with details of the debts which were "current", ie., those debts which were due for less than 30 days from an end of month summary statement, and which debts were overdue, or due for more than 30, 60 , 90 or 120 days. To the end of June 1986, all or substantially all of the company's debts to APA were paid when due. Thereafter, the company's payment performance deteriorated. At the end of July 1986, more than half the money the company owed APA was due for more than 30 days. The proportion then fluctuated but, by the end of October, had increased to about two-thirds; of a total indebtedness of about $220,000.00 in excess of $145,000.00 was overdue. During this period, a number of reminder notices were sent by APA to the company.

By 28 November, 1986, the company's account with APA was in an unusually bad state; the overdue indebtedness of about $145,000.00 was almost 60 days overdue and another substantial amount was almost 30 days overdue. Nonetheless, at that time, APA neither knew nor suspected that APA was insolvent. On 28 November, the company gave APA two cheques in respect of the indebtedness which was almost 60 days overdue, one for $80,000.00 and one for $65,847.00. APA knew that, contrary to the company's usual practice, these amounts were to be paid out of receipts by the company in respect of work which did not involve APA. Further, only the larger cheque for $80,000.00 was to be presented and met immediately. The smaller cheque for $65,847.00 was to be held by APA until the company received a further progress payment which it anticipated. On 4 December, 1986, APA was advised to hold the smaller cheque until 10 December. On that day, it was told that the cheque still could not be presented and it was not banked until 12 December.

Although APA did not know it, the company had become insolvent on 17 November 1986. However, despite that fact and

the filing of a winding-up application on 13 April 1987, the company continued to operate, including transacting business with APA, until a winding-up order was made on 17 June 1987.

APA did not dispute that it had received a "preference priority or advantage other creditors" if, as has been held, the material period for present purposes was the 6 months before the filing of the winding up application and either of the payments of 28 November 1986 was caught by section 452. The extent of the "preference, priority or advantage" depends upon whether both or one only or neither of the two payments is affected by section 451.

The first issues which arise for determination are whether either or both the payments made by the cheques delivered by the company to APA on 28 November 1986 were paid in the ordinary course of business and, if so, whether APA knew or had reason to suspect when it received the cheques that (i) the company was unable to pay its debts as they became due from its own money and (ii) the effect of payment of the cheques would be to give APA a preference, priority or advantage over other creditors. Despite sub-section 122(3) of the Bankruptcy Act, the onus of proving the circumstances giving rise to the inference referred to in sub-section 122(4) lies on the liquidator: Qld. Bacon Pty. Ltd. v. Rees (1965) 115 CLR 266; Re Weiss ex parte White v. Vicars and Co. Ltd. (1970) ALR 654.

However, although there can be some overlapping of the concepts and the same facts may be material to both (K & R Fabrications (Qld) Pty. Ltd. v. M & B Rigging Pty. Ltd. (1982) Qd.R. 585), it is for APA to establish that it received the cheques on 28 November 1986 in the ordinary course of business and, in my opinion, it failed to do so. The trial judge held that the cheque for $80,000.00, but not the cheque for $65,847.00 was received in the ordinary course of business but, on the facts of this case, I do not think that such a distinction can legitimately be drawn.

It is true that the company had previously sometimes paid

APA by means of separate cheques, including in March and May 1985, but this circumstance falls to be considered in the context of the company's practice of paying APA from progress payments received by the company from the contracts involving work or services supplied by APA. Further, apart from the two occasions referred to in early 1985, the company's use of two cheques to pay a debt to APA had been confined to the second half of 1986; prior to 28 November 1986, APA had been paid by two cheques in August and again in September 1986.

In any event, the evidence does not establish that the payments made on 28 November 1986 were made in the ordinary course of the business relationship between the company and APA or, more broadly, in the usual course of business generally, unrelated to business of any particular nature or involving any particular parties or any special considerations such as insolvency: Burns v. McFarlane (1940) 64 CLR 108; Downs Distributing Co. Pty. Ltd. v. Associated Blue Star Stores Pty. Ltd. (in liquidation) (1948) 76 CLR 463; Taylor v. White (1964) 110 CLR 129.

The cheques of 28 November 1986 involved the division of a substantially overdue liability into two components with only one immediately paid and the other postponed for what was intended to be a relatively brief but unspecified period. It is artificial to view the two cheques separately; they were given and received as part of a single transaction which was not, wholly or partially, "in the ordinary course of business". Neither cheque fully discharged the company's overdue debt nor was given "as part of the undistinguished common flow of business done, ... calling for no remark and arising out of no special or particular situation": Downs Distributing at p.477. Just as the smaller cheque was handed over in payment of an unusually long overdue debt with an arrangement that it not be immediately presented, the larger cheque was handed over in part payment of the same unusually long overdue debt accompanied by the smaller cheque for the remainder of that debt with the

arrangement referred to.

In the circumstances, it is unnecessary to consider whether APA received the cheques of 28 November 1986 in good faith, although the conclusion that the cheques were not paid in the ordinary course of business might well bear upon the question whether the inferences spoken of in sub-section 122(4) of the Bankruptcy Act should be drawn: cf Taylor v. White at p.153; Re Cummins ex parte Harris v. ARC Engineering Pty. Ltd. (1985) 62 ALR 129.

The remaining issue with respect to the two cheques received by APA on 28 November 1986 involves a decision as to the end of the "preference, priority, or advantage" period for the purpose of section 451 of the Companies Code. This is discussed in 6 above. As there indicated, the running account between the company and APA with which section 451 is concerned ended with the filing of the winding-up application.

That being so, the result of concluding that neither payment of 28 November 1986 was made in the ordinary course of business is, as was not disputed, that the amount of APA's "preference, priority or advantage" which is avoided under section 451 is increased to $108,984.79.

The remaining matter concerns the two payments made by the company to APA between the filing of the winding up application and the making of the winding up order. $12,124.00 was paid to APA by the company on 15 April 1987 to discharge a debt which arose in January 1987 and $29,478.13 was paid on 21 May 1987 in respect of a debt which arose in February 1987. By the end of April or the beginning of May, APA knew that an application for the winding up of the company had been filed. The company also had other outstanding accounts and a judgment against it. Even so, based on what it was told by the company, APA believed that the debt on which the winding up application was based had been disputed and that the dispute was resolved. APA believed that the company was solvent. Both debts paid by the company were incurred before the commencement of the winding up but paid

after the commencement of the winding up. The company and APA continued to trade up until the making of the winding up order, apparently to the net detriment to APA and benefit of APA's other creditors: the amount of the company's indebtedness to APA increased after the winding up application was filed as APA continued to supply trucks to the company which used them to continue to perform its contracts. Further, the primary judge found that the company's "rate of decline must have been substantially diminished", that the "company clearly earned income during the relevant period and ... reduced ultimate losses to a considerable extent," that it would have been difficult, if not impossible, for the company to have obtained trucks from any source except APA and that the company could not have continued to perform its work without trucks. It is a reasonable inference that APA would not have continued to supply trucks to the company but for the material payments.

Irrespective of the overall end result, continuation of the company's business after the winding up application was filed could bona fide have been perceived to be in the interests of the general body of creditors and the transactions between the company and APA were necessary for that purpose; without the payments which were made to APA, the company would not have obtained the trucks which it needed for its business operations.

In the circumstances, the liquidator's attempt to upset he judge's exercise of discretion cannot succeed.

In summary, I would allow the liquidator's appeal only to the extent of increasing the amount declared void pursuant to section 451 of the Companies (Queensland) Code to $108,984.79. Otherwise, I would dismiss the liquidator's appeal and APA's cross-appeal must also be dismissed. I would order APA to pay the liquidator's taxed costs of and incidental to the appeal and cross-appeal.

IN THE COURT OF APPEAL

SUPREME COURT OF QUEENSLAND

Appeal No. 75 of 1993

Brisbane

[Starkey v. APA Transport Pty. Ltd.]

BETWEEN:

GRAHAM LINDSAY STARKEY in his capacity as Liquidator of ALLAN FITZGERALD PTY. LTD. (IN LIQUIDATION) Appellant

- and -

APA TRANSPORT PTY. LTD. Respondent

The President
Mr Justice Pincus
Mr Justice Moynihan

Judgment delivered 20/10/93

Separate reasons for judgment by the President, Pincus JA and Moynihan SJA. Moynihan SJA agreeing with the order of the President. Pincus JA dissenting in part.

LIQUIDATOR'S APPEAL ALLOWED TO THE EXTENT OF INCREASING THE AMOUNT DECLARED VOID PURSUANT TO S.451 COMPANIES (QUEENSLAND) CODE TO $108,984.79. OTHERWISE, LIQUIDATOR'S APPEAL DISMISSED. APA'S CROSS-APPEAL DISMISSED. APA TO PAY THE LIQUIDATOR'S TAXED COSTS OF AND INCIDENTAL TO THE APPEAL AND CROSS-APPEAL.

CATCHWORDS: BANKRUPTCY - Preferences - Two cheques given to respondent within 6 months of filing of winding-up application - one not to be cashed until company gave notice - contrary to parties' usual practice, cheques to be paid from proceeds of jobs not involving respondent - other payments made after application filed but before order - "running account" principle - whether applicable to period after application filed - relationship ss.368 and 451 Companies (Queensland) Code

Counsel: Mr. W. Sofronoff Q.C. with him Mr. Lilley for the appellant/cross-respondent
Mr. P. Keane Q.C. with him Mr. D. North for the respondent/cross-appellant

Solicitors: Sly & Weigall for the appellant/cross-respondent
John P. Kelly for the respondent/cross-appellant

Hearing Date: 04/08/93

IN THE COURT OF APPEAL

SUPREME COURT OF QUEENSLAND

Appeal No. 75 of 1993.

Brisbane

[Starkey v. APA Transport]

BETWEEN

GRAHAM LINDSAY STARKEY in his capacity as Liquidator of ALLAN FITZGERALD PTY LTD (IN LIQUIDATION)

Appellant

- and -

APA TRANSPORT PTY LTD

Respondent

REASONS FOR JUDGMENT - PINCUS J.A.

Judgment delivered 20/10/93.

This is an appeal and cross-appeal challenging orders made in the Supreme Court, concerning the winding-up of an insolvent company ("Fitzgerald PL"). The orders challenged in this Court dealt with two categories of issues.

First, there was a dispute as to whether two payments made by cheque to a creditor ("APA") on 28 November 1986 for $80,000 and $65,847.35 were voidable preferences; as to those, the appellant liquidator succeeded with respect to the smaller cheque. However, because, as was common ground, the matter was to be determined on a "running account" basis, the amount ordered to be repaid by APA was $38,837.59 (plus interest) only.

The second category of issues related to payments made by Fitzgerald PL to APA during the period between the filing of an application for winding-up, which occurred on 13 April 1987, and the order for winding-up of 23 June 1987. The judge granted an order under s. 368(1) of the Companies (Queensland) Code ("the Code") validating those payments and the liquidator's appeal seeks to have that order upset.

Four questions, according to the argument of Mr Sofronoff QC, who led for the liquidator, require to be resolved:

1. Did APA have reason to suspect, on 28 November 1986 when the two cheques were delivered to it, that Fitzgerald PL was insolvent?
2. Were the two cheques paid in the ordinary course of business?
3. (If either question 1 or question 2 is answered favourably to the liquidator): Is the extent of the preference to be determined on a "running account" basis by examining the state of the accounts at the commencement of the winding-up or, on the other hand, at the date on which mutual trading ceased?
4. Was the judge justified in exercising his discretion, on the issue of validation, in favour of APA?

The mutual trading consisted in APA's supplying trucks at hourly rates to Fitzgerald PL, for use in the latter's business as an engineering contractor. APA used to submit invoices for truck hire from time to time and at the end of each month would provide a statement summarising the amounts which had fallen due during that month. The understanding was that payment was to be made to APA within 30 days from the end of the month in which the invoices were sent. When the two cheques of 28 November 1986 were given to APA, Fitzgerald PL was insolvent, but APA did not know that; the judge held, in favour of APA, that it did not then have reason to suspect insolvency, either. However, the judge held that the smaller of the two cheques of 28 November 1986 was not paid in the ordinary course of business, so that the liquidator succeeded on that point.

As I have explained, the liquidator attacked only two payments made to APA. Between the date of those payments and the application for winding-up, two other substantial payments were made which were not challenged. That was because, the Court was told, the result of the running account principle was that neither of the two later payments produced a preference.

ISSUE 1

The preference aspect of the case depends on s. 451(1) of the Code which reads in full as follows :

> "451(1). A settlement, a conveyance or transfer of property, a charge on property, a payment made, or an

> obligation incurred, by a company that, if it had been made or incurred by a natural person, would, in the event of his becoming a bankrupt, be void as against the trustee in the bankruptcy, is, in the event of the company being wound-up, void as against the liquidator.
>
> 451(2). For the purposes of sub-section (1), the date that corresponds with the date of presentation of the petition in bankruptcy in the case of a natural person is -
>
> a) in the case of a winding-up by the Court -
>
> ...
>
> iii) in any other case - the date of the filing of the application for the winding-up.
>
> 451(3) For the purposes of this section, the date that corresponds with the date on which a person becomes a bankrupt is the date on which the winding-up of the company commences or is deemed to have commenced.

The bankruptcy provision which is picked up by s. 451 is s. 122 of the Bankruptcy Act 1966; it is unnecessary to set the terms of that familiar provision out. The principal features for present purposes are as follows :

(i) It operates on a payment made to a creditor by a person unable to pay his debts as they become due from his own money; that condition is satisfied with respect to both cheques.

(ii) The payment must have the effect of giving that creditor an advantage over other creditors; there is a dispute as

to the effect of that requirement in the present case.

(iii) The rights of a payee "in good faith and for valuable consideration and in the ordinary course of business" are protected; there is a dispute as to whether the payments were in the ordinary course of business.

(iv) The protection mentioned in (iii) is not available if the payment was made under such circumstances as to lead to the inference that the creditor knew, or had reason to suspect that the debtor was unable to pay his debts as they became due from his own money, and that the effect of the payment would be to give him a preference, priority or advantage over other creditors; there is a dispute about this aspect.

The primary judge accepted that Fitzgerald PL had at relevant times very substantial construction projects. In 1985 and 1986 it had a large job at the Brisbane Domestic Airport which produced substantial payments to it; that drew to a close in the latter part of 1986. Fitzgerald PL often paid its trade

creditors, such as APA, out of progress payments which it received and the tendency was to pay a creditor from progress payments which included the work that creditor had done or services it had provided.

The material before the Court includes a list of APA debtors for each of the months from January 1986 to June 1987. It will be recalled that the critical date is 28 November 1986. The lists include a summary of the age of the debts, in various categories: those which are "current", those overdue for 30 days, for 60 days, for 90 days and for 120 days or more. The "current" debts are those which have not been due for as long as 30 days -i.e. 30 days since the monthly statement was sent.

An examination of these lists indicates that, considering APA's debtors generally, there does not appear to have been any rigid insistence upon prompt payment; this assists APA's case. A useful index of the creditor's policy is the percentage of "current" debtors in each month. In respect of the 12 months beginning January 1986 the percentages were 55, 46, 36, 52, 47, 64, 36, 41, 55, 39, 39 and 50 respectively. It is, however, of assistance to the liquidator that the performance of Fitzgerald PL, as a debtor of APA, deteriorated during the course of that year. Each statement in the first six months of 1986 shows that there was either nothing or substantially nothing overdue. At the end of July 1986 more than half the money Fitzgerald PL owed

APA was more than 30 days overdue; at the end of September about a third was more than 30 days overdue and at the end of October about two-thirds was more than 30 days overdue. This change in the pattern of payment by Fitzgerald PL provided some reason for concern in APA. Further, there was evidence that APA had a system of sending reminders in respect of sums overdue and that Fitzgerald PL received a number of such documents at relevant times.

The criticisms which were advanced by Mr Sofronoff of the judge's conclusion with respect to the two cheques were based on a number of specific points. He argued that the two cheques paid on 28 November 1986 were in a special category, because the funds being used to make those payments came from jobs with which APA had no involvement. As I have mentioned, the evidence was that generally the practice was otherwise; moneys paid to creditors such as APA would be derived from progress payments on jobs to which the creditor had contributed work or services. Therefore, it was argued, those sums must have been paid at the expense of other creditors who would in the ordinary course have been paid out of the moneys used to pay APA. Mr O'Donnell, who dealt with Fitzgerald PL on behalf of APA, made an entry in his diary which evidenced that the money in question came from a job APA had not "worked on". However, the point seems to me to be, by itself, not a matter of great significance. There is no evidence that Mr O'Donnell was told why the unusual course I

have mentioned was being followed; for all he knew, there may have been a sufficient surplus in the payments made to Fitzgerald PL to allow for the payments to APA, as well as others which would according to ordinary practice be paid.

Next, Mr Sofronoff argued in effect that the judge did not give enough weight to the unusual state of the accounts between Fitzgerald PL and APA on 28 November, 1986. It was pointed out that at the end of October 1986 over $145,000 was 30 days overdue, of a total sum then due of about $220,000. It is true that, as was argued for the appellant, that was an unusually bad position. It is also correct that the two cheques in question, paid almost at the end of the ensuing month, discharged a liability which was then almost 60 days overdue. It was further pointed out that payment of those cheques left the position even worse at the end of November 1986, because by then about $65,000 was 60 days overdue.

That was so, because of an arrangement which was made between the parties. Mr O'Donnell's evidence was to the effect that he agreed with Mr Allan Fitzgerald on behalf of Fitzgerald PL that the $65,847 cheque was to be held until Fitzgerald PL received a progress payment; Mr O'Donnell thought that was from a job at Callide. Six days later, on 4 December, Mr O'Donnell "probably had advice", according to the judge's finding, to hold the smaller cheque until the following Wednesday, 10 December.

On that day, the evidence shows, Mr O'Donnell rang to inquire whether he could bank the second cheque and was told he could not. It was in fact banked on Friday 12 December.

Mr Sofronoff argued that the combination of circumstances - that APA was to hold the second cheque until a date not precisely specified; that the state of accounts on 28 November was unusually bad; and that APA knew that the money it was receiving was not coming from jobs in which it was involved - amounted to a case which, looking at the matter objectively, must have given a reasonable person in Mr O'Donnell's position a suspicion that Fitzgerald PL could not pay its debts.

One answer is that there was evidence that on previous occasions, when there was no question of insolvency, a payment made by Fitzgerald PL to APA had been split in similar fashion. The learned primary judge placed "no particular significance" on that circumstance, but it appears to me to have relevance. In Mr O'Donnell's evidence, which does not appear to have been disputed on this point, a number of occasions were identified when that had happened. Mr O'Donnell also said that Mr Fitzgerald had given him cheques which he was asked not to present until he was notified that Fitzgerald PL had received certain payments.

Notwithstanding that, there was plainly room for an

inference against APA with respect to the issue of suspicion of insolvency. The view the judge seems to have taken of the matter was that the liquidity of Fitzgerald PL fluctuated from time to time, depending on the timing of the payments it received. His Honour also took into account, in favour of APA, that its previous dealings with Fitzgerald PL and in particular with Mr Fitzgerald had been satisfactory, in the sense that arrangements it made to pay APA were carried out. No cheques were ever dishonoured and Mr Fitzgerald was "always very reliable with respect to making payments in accordance with any...discussions with him". The judge said that :

> "At worst for the company, the delay in presentation of the second cheque to 12 December 1986 merely showed a temporary shortage of liquid funds although it was equally open to an inference that the company preferred to pay accounts out of liquid funds rather than from other sources."

The statement I have quoted is at least incomplete, in that at the time at which the judge was speaking the company was in fact insolvent, as is conceded. His Honour must be taken to have meant that the delay in presentation of the second cheque might reasonably (although not in fact accurately) have been taken by APA to reflect a mere temporary shortage of funds. It is difficult to see why his Honour was not entitled, in the whole of the circumstances, to take that view.

The question posed by the statute is whether the circumstances were such as to lead to the inference that the creditor had reason to suspect that the debtor was "unable to

pay his debts as they became due from his own money". Although the matter must be close to the border line, I am of opinion, on the whole, that the conclusion at which the judge arrived is a defensible one and should not be upset.

ISSUE 2

The next point of attack on the judgment relates to the issue of "ordinary course of business". As has been explained, the judge reached different conclusions in respect of each of the two cheques, although handed over on the same day. That is at first sight an unusual course, and a question arises whether what happened with respect to the smaller cheque "infected" the larger.

One starts, logically, with the challenge to the judge's conclusion relating to the smaller cheque. What his Honour said, in summary, is as follows. His Honour took the view that the Court "does not look at the particular business or course of dealings between the parties, but the general flow of the ordinary course of business". He acknowledged that one must look at the "circumstances of the particular case", but said this did not include the state of mind of the payer.

His Honour did not place significance on the general history of the dealings between the parties, nor on the fact that the account was overdue for payment in accordance with

normal terms. The judge thought it to be "somewhat unusual" that a cheque currently dated would be handed into the care of the creditor, under the arrangement made, and held that the combination of circumstances "called for comment and did not fall into place as part of the undistinguished common flow of business".

There may be room for argument with respect to the nature of the test to be applied. That which is most commonly used and was relied on by the primary judge is succinctly expressed by Rich J in Downs Distributing Company Pty Ltd v. Associated Blue Star Stores Pty Ltd (In Liquidation) (1948) 76 C.L.R. 463 at 47:

> "...the transaction must fall into place as part of the undistinguished common flow of business done, that it should form part of the ordinary course of business as carried on, calling for no remark and arising out of no special or particular situation."

It appears to me that the judge applied that test correctly. It is true that much broader tests find support in the authorities: e.g. Robertson v. Grigg (1932) 47 C.L.R. 257 at 267; but the advantage of what I believe now to be the more orthodox test is that it is more certain and clear in its application than others. It appears to me that general considerations such as the "fairness" of a payment should have little to do with whether it is in the ordinary course of business, although they may be relevant to the requirement of good faith. It is clear from the very terms of s. 122 that a

payment may be made and received in all good faith and yet be a preference; it should be added that here, good faith is not in question.

There was evidence, as I have explained, that on previous occasions payments had been made at or about the same time by more than one cheque and that on previous occasions cheques paid had been a subject of requests to defer presentation. Nevertheless, it seems to me impossible to upset the conclusion of the primary judge that the circumstances in which the smaller cheque was paid were not "in the ordinary course of business". It is true that the decision of the High Court in Queensland Bacon Pty Ltd v. Rees (1966) 115 C.L.R. 266 appears to support the view that dishonour of a cheque does not necessarily render a subsequent payment one other than in the ordinary course of business; but to hand over a cheque in payment of a sum unusually long overdue, associating with it an arrangement that it is not to be presented until some date in the future (not then fixed) appears to me, viewed objectively, to be outside the ordinary course of business.

There remains to be considered whether the facts relating to the smaller cheque destroy the judge's conclusion as to the larger ($80,000) cheque. Considered in isolation, that was simply a partial payment of moneys due and it does not appear to me right to judge it by reference to the arrangement made about

the other cheque delivered on the same day; the $80,000 cheque was not subject to or conditional upon anything relating to the other cheque. Therefore, on this aspect of the matter also, I agree with the primary judge's conclusions.

ISSUE 3

The third issue relates to the working of the "running account" principle, the operation of which is established and illustrated by the decisions of the High Court in Richardson v. The Commercial Banking Company of Sydney Limited (1952) 85 C.L.R. 110 and Rees v. Bank of New South Wales (1964) 111 C.L.R. 210. Although s. 122 of the Bankruptcy Act 1966, discussed above, does not expressly say so, it is construed as requiring consideration of the whole of the transaction, where a payment which is impugned "forms an integral, an inseparable, part of an entire transaction" : Richardson's case at 129. In Rees :

> "...the arrangements made between the bank and the company from time to time during the period were such that by a common business purpose of the company and the bank each deposit was so connected with subsequent payments out that the question whether the deposit had the effect of giving the bank a preference was to be decided not by considering its immediate effect only but by considering what effect it ultimately produced in fact."

It is the word "ultimately" which is critical. If the argument of Mr Keane QC for the respondent/cross-appellant, is correct, then one must consider the running account between the debtor and the creditor right up to the cessation of trading, which carried on well past the date of the commencement of the

winding-up, 13 April 1987. That is, between that date and the order for winding-up (23 June 1987), the balance due increased and it would be of assistance to the respondent (APA) to have it held that one considers at the date of cessation of trading the extent of the preference given by payment of the cheque for $65,847.35. If this were the case, the extent of the preference would effectively be nil, and no repayment would be required.

It was argued for the appellant liquidator, in accordance with the view of the primary judge, that a running account is to be considered only up to the date of filing the application for winding-up, the validity of later payments being governed by s. 368(1) of The Companies (Queensland) Code, which makes any disposition of the property of the company after the commencement of the winding-up void, unless the Court otherwise orders. Under s. 368(2) the Court has power to validate the making of a disposition of the property of the company after the filing of an application for winding-up.

There is authority which perhaps tends against the view taken by the primary judge, on this point : Re Discovery Books Pty Ltd (1972) 20 F.L.R. 470 at 474-5. There, in discussing a passage from Richardson's case, Fox J said :

> "What I understand from the passage cited is that the effect of a payment is to be judged after bankruptcy, with due regard for events occurring after the payment was made, and that one must ultimately come back to considering whether by reason of the payment, or dealing, there is less money available for the

general body of creditors than otherwise might have been expected to be the case".

If one were to apply that dictum quite literally, it would suggest that the payment here impugned must be judged, as to its preferring effect, by the ultimate outcome, at and even after winding-up. But Tellsa Furniture Pty Ltd (In Liquidation) v. Glendave Nominees (1987) 9 N.S.W.L.R. 254 at 261-2 and National Acceptance Corp. Pty Ltd v. Benson (1988) 6 A.C.L.C. 685 are to the contrary. In Putnin v. Energy Trucking Pty Ltd (Supreme Court of W.A.) (1990) 8 A.C.L.C. 485 consideration was given to the question whether s. 451 can have effect upon transactions entered into or payments made after the application to wind-up. Tellsa Furniture was discussed, as was the consideration of that case in the Full Court of the Supreme Court of Queensland in re Allan Fitzgerald Pty Ltd (1989) 7 A.C.L.C. 1188. Murray J suggested in Putnin that what was said in Tellsa was "a distortion of the general statutory policy otherwise to be detected from the recognition within the Companies Code of the principle that debts ranking equally should be paid pari passu and that undue preferential payments...should be void without a capacity for validation in the Court...".

But subsequent authorities have taken the same line as was adopted in Tellsa : Sheahan v. Workers Rehabilitation and Compensation Corporation (1991) 9 A.C.L.C. 1303, re Transconsult Australia Pty Ltd (1991) 9 A.C.L.C. 1052.

In my opinion, the correct view is that transactions entered into or payments made after commencement of the winding-up, which are prima facie void whether or not they give a preference, are not liable to be attacked under s. 451. This appears to me to be in accordance with the weight of authority and to have the advantage of avoiding the complexity of requiring post-commencement payments to overcome two hurdles rather than one. In the present case, no attack under s. 451 is made on post-commencement payments, but it is sought to have them taken into account, along with the post-commencement debits in applying s. 451 to the two impugned payments. I think this is not permissible and that the running account principle is properly applied by regarding the account as having ceased for the purposes of s. 451 at the commencement of winding-up; that is the view the judge took.

I am therefore of opinion that the judge's view that payments after commencement of the winding-up were to be considered solely under s. 368 is correct.

ISSUE 4

This is the attack on the exercise of the judge's discretion under s. 368 of The Companies Code. The judge held that the continuance of the provision of trucks by APA was an essential component of the ability of the company to continue

with its projects. If APA had ceased to supply, so the judge found, it would have been very hard if not impossible for Fitzgerald PL to get other trucks. The payments in question could, at the time they were made, reasonably be perceived as offering some advantage or potential advantage to the company or its general body of creditors.

In Tellsa Furniture (above) the submission that a payment which would in any event be a preference would not be validated was rejected. There, goods supplied after the commencement of winding-up were incorporated in what the debtor company sold and the proceeds of sales were used to keep the company going. It was held by Priestly JA that the Court would not validate a payment discharging an unsecured pre-liquidation debt except in special circumstances and that dispositions made in the ordinary course of business will generally be validated as long as they relate to the continuation of business and the earning of income or saving of loss during the pendency of the winding-up application, as opposed to merely reducing a pre-existing debt.

It is necessary to avoid being too broad, since the circumstances can vary infinitely, but a Court should not in my opinion be overly willing to refuse to validate payments made to a creditor which continues to trade with the debtor company after the commencement of winding-up, in circumstances where the continuation of trade and the making of the payments, appear to

have some real prospect of enabling the debtor company to survive. Here, it was argued, and I think correctly, that it was not proved that the payments made in fact provided any benefit for the general body of creditors. But if payments of this kind are, in general, not to be validated then the incentive a creditor might otherwise have to assist the debtor to continue to carry on will be substantially reduced. One reason why, in my view, the judge's exercise of discretion can be said to have produced a sound result is that continuing to trade after the commencement of winding-up seems to have harmed APA. The amount due to it increased substantially between the commencement of the winding-up and the cessation of trading. But it is my opinion that the exercise of discretion by the judge has not been shown to have been based upon application of a wrong principle and that it should be upheld.

The appeal and cross-appeal should be dismissed, each with costs.

IN THE COURT OF APPEAL

SUPREME COURT OF QUEENSLAND

Appeal No. 75 of 1993

Brisbane

Before The President
Mr Justice Pincus
Mr Justice Moynihan

BETWEEN

GRAHAM LINDSAY STARKEY in his capacity as Liquidator of ALLAN FITZGERALD PTY LTD (IN LIQUIDATION)

Appellant

- and -

APA TRANSPORT PTY LTD

Respondent

REASONS FOR JUDGEMENT - MOYNIHAN SJA

The relevant facts and statutory provision are adequately canvassed in the judgments of Fitzgerald P and Pincus JA which I have had the advantage of reading. It is unnecessary for me to rehearse them here.

I agree with Fitzgerald P that it is artificial to the extent of being inappropriate to regard the two cheques paid by Allan Fitzgerald Pty Ltd (in liquidation) to APA Transport Pty Ltd on 28 November, 1986 as constituting separate transactions. I agree with Fitzgerald P's reasoning and consequent conclusion that the cheques are to be regarded as given and received in a single transaction which was not wholly or partially in the ordinary course of business. Otherwise I agree with the reasons of Fitzgerald P and Pincus JA. I agree with the orders proposed by Fitzgerald J.