

# SUPREME COURT OF QUEENSLAND

CITATION: *Erol v Cavus and Ors* [2012] QSC 371

PARTIES: **MEHMET EROL** (in his own capacity and as trustee of the Erol Family Trust)  
(Plaintiff)

**v**

**YUSUF CAVUS** in his own capacity and as executor of the estate of the estate of HABIL EROL (deceased)  
(First Defendant)

**AND**

**MUHARREM NUREDDIN COSAN**  
(Second Defendant)

**AND**

**KOTKU BREAD PTY LTD (ACN 089 980 772)**  
(Third Defendant)

**AND**

**FILLA BAKERY PTY LTD (ACN 145 938 450)**  
(Fourth Defendant)

FILE NO/S: BS 7107 of 2008

DIVISION: Trial

PROCEEDING: Application

ORIGINATING COURT: Brisbane

DELIVERED ON: 23 November 2012

DELIVERED AT: Brisbane

HEARING DATE: 13 September 2012

JUDGE: Boddice J

ORDER:

CATCHWORDS: CORPORATIONS – VOLUNTARY ADMINISTRATION – DEEDS OF COMPANY ARRANGEMENT – TERMINATION OR AVOIDANCE – where the third defendant carried on a wholesale bakery business – where the third defendant, by resolution of its director, appointed administrators – where creditors of the third defendant approved a Deed of Company Arrangement – where the plaintiff, as a shareholder and creditor of the third defendant, seeks the winding up of the third defendant on the grounds of

oppressive conduct or on the just and equitable ground – where the defendants and deed administrators oppose the termination of the administration – where the administrators also seek the discharge of a restraining order made by consent so as to allow them access to funds for distribution to unrelated creditors in accordance with the terms of the Deed – whether the Deed should be terminated – whether the restraining order should be discharged

*Corporations Act 2001 (Cth)*, ss 436A, 444DA(5), 445D, 445G, 447A

*Blacktown City Council v MacArthur Telecommunications Pty Ltd* [2003] NSWSC 883

*Kotku Bread Pty Ltd v Vero Insurance Ltd & Anor* [2012] QSC 109

COUNSEL: P W Hackett for the plaintiffs  
C A Johnstone for the first, second and fourth defendants  
S J Webster, on direct access brief, for the deed administrators of the third defendant

SOLICITORS: PM Lee & Co for the plaintiffs  
Bennett & Philp Lawyers for the first, second and fourth defendants

- [1] **Boddice J:** By application filed 16 July 2012, the plaintiff seeks orders pursuant to s 447A of the *Corporations Act 2001 (Cth)* (“the Act”) terminating the administration of the third defendant, and the winding up of the third defendant.
- [2] By amended application filed 12 September 2012, the administrators of a Deed of Company Arrangement (“the Deed”) for the third defendant seek a declaration, pursuant to s 445G of the Act, that the Deed is valid and an order, pursuant to s 444DA(5) of the Act, approving the Deed insofar as it varies priority entitlements for certain employees. The administrators also seek the discharge of a restraining order made, by consent, on 22 February 2012, so as to allow them access to funds for distribution to unrelated creditors in accordance with the terms of the Deed.

## Background

- [3] The present proceedings were commenced by the plaintiff on 25 July 2008. He seeks various forms of relief as a consequence of what he alleges is oppressive conduct by his late brother and the second defendant in conducting the business of the third defendant to his exclusion. Relevantly to this application, the plaintiff, as a shareholder and creditor of the third defendant, sought the winding up of the third defendant, either due to oppressive conduct or on the just and equitable ground.

- [4] The third defendant, and the first and second defendants, have, since the commencement of these proceedings, resisted any winding up of the third defendant.
- [5] The third defendant carried on a wholesale bakery business at Capalaba from 2005. The plaintiff, the second defendant and the estate of Habil Erol, the plaintiff's brother, each own one issued share in the third defendant. The first defendant is the trustee of Habil Erol's estate, and a director of the third defendant.
- [6] On 19 August 2010, the third defendant's factory was destroyed by fire. The fourth defendant was incorporated on 23 August 2010, some four days later. It carries on a similar business of a wholesale bakery, from premises at Yatala in the State of Queensland. Initially, its directors were the first and second defendant and a Mr Tombuloglu. The first defendant resigned as a director in November 2010. The plaintiff alleges the fourth defendant has, with the assistance of, and under the direction of, the first and second defendants, conducted the business of a wholesale bakery formerly operated by the third defendant, at different premises.<sup>1</sup>
- [7] The land on which the third defendant's factory was located was owned by the plaintiff, his late brother and the second defendant. The factory building was insured under a policy of insurance. The contents of the factory were insured under a different policy. The beneficiary of the contents policy was the third defendant.
- [8] Following the fire, the third defendant sought, but was denied, indemnity by its insurer. The third defendant subsequently commenced proceedings against its insurer and its insurance broker.
- [9] The trial of the third defendant's claim commenced on 13 February 2012. On 14 February 2012, the plaintiff made application for restraining orders in respect of any assets of the third defendant pending the trial of this proceeding.
- [10] On 22 February 2012, the parties consented to orders restraining the third defendant from dealing with its assets except in specified circumstances. The consent order applied to any funds received by the third defendant pursuant to its claim against the insurer and its insurance broker.
- [11] On 20 March 2012, Perpetual Nominees Limited ("Perpetual"), the major creditor of the third defendant, served a statutory demand on the third defendant, and threatened winding up proceedings if the debt was not paid by 4 July 2012.
- [12] On 26 April 2012, Applegarth J gave judgment for the third defendant against the insurance broker in respect of the third defendant's claim.<sup>2</sup> On that same day, the third defendant granted registered charges in favour of the first and fourth defendants. These charges were granted without the knowledge of the plaintiff.

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<sup>1</sup> Fourth Amended Statement of Claim, paragraphs 25 and 26.

<sup>2</sup> *Kotku Bread Pty Ltd v Vero Insurance Ltd & Anor* [2012] QSC 109.

- [13] In accordance with the judgment in the proceedings against its insurance broker, the third defendant received an amount of \$3,140,790.78. This sum was paid into the Trust Account of its solicitors as required by the terms of the restraining order.
- [14] As a consequence of the consent order made 22 February 2012, the proceeds of that judgment are frozen, with the third defendant being restrained from dealing with those proceeds, except to pay:
- (a) its secured creditors in full;
  - (b) itself, the first defendant and the second defendant for legal costs paid by them in the insurance proceedings; and
  - (c) the first defendant as remuneration for work performed by him in his position as managing director of the third defendant, and other employee entitlements, subject to certain notification requirements.
- [15] On 8 June 2012, the third defendant applied to vary the restraint to permit a number of payments said to have been incurred in the course of its business. Those payments included payments to Perpetual, the Australian Taxation Office and the fourth defendant. That application was refused on 27 June 2012. In so doing, the Chief Justice noted the obvious intent behind the restraining order was “to protect those funds so that they would be available to meet any judgment given in the current proceeding in favour of the plaintiff”. The Chief Justice also observed that at the time the order was consented to, the parties were aware of the liabilities owed by the third defendant, including the large sum owed to Perpetual.
- [16] On 4 July 2012, the third defendant, by resolution of its director, and without prior notice to the plaintiff, appointed administrators pursuant to s 436A of the Act. That date was the date Perpetual had given as the last date for payment of the sum owing pursuant to the statutory demand served on the company in March 2012.
- [17] On 9 July 2012, the administrators published a report to creditors which identified creditors, including the plaintiff, in the sum of \$3,401,858.38. In that report, the administrators recommended creditors resolve to accept the Deed put forward by the first and fourth defendants.
- [18] Prior to the meeting of the creditors, the plaintiff’s solicitors wrote to the administrators asserting the Deed was unfair to the plaintiff and his wife, was a fraud upon the administration power, and would result in the entire deficiency in the company being met by the plaintiff and his wife. The plaintiff’s solicitors also highlighted the advantages of liquidation over administration and how the liquidation would treat creditors equally.
- [19] On 16 July 2012, the plaintiff’s application to end the administration was filed with this court. Whilst it was returnable on 30 July 2012, the application was adjourned on that date to permit a meeting of creditors to take place. On 22 August 2012, the second meeting of creditors, by a majority, approved the Deed.

## **The Deed**

- [20] The Deed provides for the administrators to make an admitted list of claims, including employee entitlements. Subject to the terms of the Deed, the administrators must not make any distribution to admitted creditors unless the administrators are satisfied there are, or will be, sufficient funds to pay the administrators' remuneration, any outstanding debts and obligations incurred by the administrators, and all employee entitlements pursuant to s 556(1)(e)-(h) of the Act.
- [21] The Deed further provides that the administrators must not make a distribution or payment to Perpetual, as an admitted creditor, unless Perpetual agrees to assign to the administrators its rights, title and interest to the Perpetual debt and related agreements.
- [22] The Deed further provides that the administrators are to use the funds the subject of the restraining order to pay the admitted creditors. The Deed is conditional upon the administrator applying for orders releasing those funds, and declaring that the Deed is valid.
- [23] The Deed expressly deals with the claims of the plaintiff in this proceeding, including any claims for employee entitlements, and any claims made by the first and fourth defendant, including any employee entitlements. The claims made by the plaintiff will be deferred, and dealt with in the Supreme Court proceedings, whilst the claims by the first and fourth defendant will be postponed pending determination of those proceedings. The employee entitlements of the plaintiff and the first defendant are to be held by the administrators, and paid into a separate account as priority employee entitlements pending determination of this proceeding.

## **Plaintiff's submissions**

- [24] The plaintiff contends the winding up of the third defendant is inevitable, as it has been insolvent since the 2010 fire, has not carried on business since that time, and has no real prospect of returning to commercial life given the fractious relationships between its members. The plaintiff submits that the object of Part 5.3A of the Act is not served by continuation of the administration of a company which will, inevitably, be wound up.
- [25] The plaintiff further submits the provisions of Part 5.3A are being abused in all the circumstances. The third defendant has made inappropriate use of the Act's administration power, as there is no better return to the third defendant's creditors or members under administration than would be the case under liquidation. Further, the administration discriminates against the plaintiff and his wife in relation to priority employee entitlements and unsecured creditor claims. Finally, enabling liquidators to scrutinise and set aside uncommercial transactions would benefit the third defendant's creditors and members.

- [26] The plaintiff claims a report published by the administrators, and given to creditors before the Deed was approved, misstated the position in relation to the employee entitlements of the plaintiff and his wife. The plaintiff submits the Deed should be terminated pursuant to s 445D of the Act because the creditors voting on the Deed were misled by that report, and the plaintiff and his wife were unfairly prejudiced by the report.
- [27] Finally, the plaintiff submits that should the Deed be permitted to continue, and the relief sought granted, the plaintiff and his wife would be further discriminated against as the security created in their favour by the restraining order would be eroded, and the Deed is intended to circumvent the decision of the Chief Justice and to avoid an earlier relation back date.

### **Defendants' submissions**

- [28] The defendants oppose the plaintiff's application. They submit the Deed does not alter the priority payments as they relate to eligible employees, and the plaintiff and his wife suffer no unfairness. The plaintiff's wife will be paid in priority as an eligible employee once her claims are accepted by the administrators. The plaintiff's entitlement is quarantined pending determination of the amount payable to him.
- [29] The defendants contend that should a liquidator be appointed, the costs of scrutinising uncommercial transactions, and the potential associated litigation, would result in creditors who would have been paid under the Deed not being paid in any foreseeable time frame, and perhaps not receiving the 100 cents in the dollar they would receive under the Deed.
- [30] The defendants contend the administrators' application ought to be granted, as the Deed has the support of a majority of creditors, and will result in the creditors receiving 100 cents in the dollar. They also contend there was no material misleading of the creditors in all the circumstances.

### **Administrators' submissions**

- [31] The Deed administrators also oppose the plaintiff's application. The administrators contend there is no scope to terminate the Deed pursuant to s 445D, as the error in the administrators' report could not reasonably have been expected to have been material to the creditors in deciding whether to vote in favour of the Deed. The majority of creditors would have voted for the Deed even without the report's misstatement.
- [32] The administrators further contend the Deed achieves a better result than liquidation, as legal costs associated with proving disputed debts and investigations of insolvent transactions may result in a liquidator declaring a partial dividend. Under the Deed, the majority of creditors are immediately paid 100 cents in the dollar. This is possible as any potential costs order against the administration is

likely to be far less than the scope of the likely costs of a liquidator. The Deed provides for the parties to run any litigation themselves, not the Deed administrators. The Deed also preserves the possibility of the third defendant resuming trading.

- [33] The administrators contend there is justification for treating the disputed claims of the plaintiff and the first defendant differently from the unrelated creditors. There is a risk of delay in the payment of unrelated creditors because of this dispute. Under the Deed, the unrelated creditors get paid straight away, and there is enough money to pay the parties in dispute as soon as the disputes are resolved.
- [34] The administrators deny the Deed is unfairly prejudicial to the plaintiff in deferring his claims. All employee entitlements are paid in priority to other claims.<sup>3</sup> The plaintiff's wife's claim is not postponed. The plaintiff, like other related party creditors, will be paid as soon as the Court is satisfied he is entitled to the amount claimed, and the Deed provides for the quarantining of that amount. In a liquidation, the plaintiff's entitlement would most likely be challenged by the liquidator,<sup>4</sup> and would not be paid any sooner. The administrators also dispute the plaintiff's claim there would be insufficient funds to pay the related party claims once determined.
- [35] The administrators submit the relation back date is a non-issue, as the only unreasonable transactions identified by the plaintiff occurred in 2010. A change in relation back date would not affect the ability to investigate these transactions.

### **Legislative power**

- [36] The court has a general power to make such orders as it thinks appropriate in relation to a particular company.<sup>5</sup> That general power includes a power to order that the administration is to end if the court is satisfied that the provisions of the Part are being abused, or for some other reason.<sup>6</sup>
- [37] The Court also has power, pursuant to s 445D of the Act, to terminate the Deed. Relevantly, that section provides:
- “(1) The Court may make an order terminating a deed of company arrangement if satisfied that:
- (a) information about the company's business, property, affairs or financial circumstances that:
- (i) was false or misleading; and
- (ii) can reasonably be expected to have been material to creditors of the company in deciding whether to vote in favour of the

<sup>3</sup> DOCA, Clause 14.1(a)(iii).

<sup>4</sup> Affidavit of IA Currie, sworn 11 September 2012, paragraphs 18-22.

<sup>5</sup> *Corporations Act 2001* (Cth), s 447A.

<sup>6</sup> *Ibid.*

- resolution that the company execute the deed;
- was given to the administrator of the company or to such creditors; or
- (b) such information was contained in a report or statement under subsection 439A(4) that accompanied a notice of the meeting at which the resolution was passed; or
  - (c) there was an omission from such a report or statement and the omission can reasonably be expected to have been material to such creditors in so deciding; or
  - (d) there has been a material contravention of the deed by a person bound by the deed; or
  - (e) effect cannot be given to the deed without injustice or undue delay; or
  - (f) the deed or a provision of it is, an act or omission done or made under the deed was, or an act or omission proposed to be so done or made would be:
    - (i) oppressive or unfairly prejudicial to, or unfairly discriminatory against, one or more such creditors; or
    - (ii) contrary to the interests of the creditors of the company as a whole; or
  - (g) the deed should be terminated for some other reason.”

## Discussion

- [38] In determining whether it is appropriate to terminate the present Deed, it is important to keep in mind the object of Part 5.3A. That object encompasses several purposes. One purpose is to allow time for consideration of reconstruction possibilities so as to allow the company to return to operating its commercial business. Another purpose, if that is not possible, is to allow a procedure which will result in a better outcome for creditors.<sup>7</sup>
- [39] In considering those purposes it is important to have regard to the circumstances in which this Deed was entered into by the third defendant.
- [40] The third defendant has not been carrying on a business activity for almost two years. Its previous business of a wholesale bakery has effectively been undertaken since that date by the fourth defendant. Against that background, the Deed cannot practically involve any element of commercial rehabilitation and resumption of business activities.

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<sup>7</sup> *Blacktown City Council v MacArthur Telecommunications Pty Ltd* [2003] NSWSC 883 at [19].



- [41] The first and fourth defendants only appointed administrators when faced with the prospect of the liquidation of the third defendant due to non-compliance with the statutory demand served by Perpetual. A liquidation would result in an investigation of past transactions, including the transactions involving the payment of large sums by the third defendant to the first and second defendants and related entities in July and August 2010.
- [42] Prior to the third defendant being placed into administration, the plaintiff obtained a restraining order. Its purpose was to ensure the third defendant's funds were available to meet any judgment in his favour.
- [43] The Deed is dependent upon the administrators obtaining the funds the subject of the restraining order. To allow the Deed to continue requires this court to release the funds. That would result in the loss of the protection afforded to the plaintiff in respect of any judgment in the oppression proceedings. That is the relief which was expressly refused by the Chief Justice, for good reason.
- [44] Whilst administration will result in the payment of all unrelated creditors in full, and liquidation may result in those payments being deferred for some time, with a risk the liquidator would be involved in litigation, thereby dissipating the extent of the third defendant's available assets for distribution to its creditors, the majority of the company assets will be disbursed by the administrators in payment of the other debts. In that event, there is a significant risk there will not be sufficient funds remaining to meet the plaintiff's claims in these proceedings should the plaintiff be completely successful in those claims.
- [45] Balancing all of the circumstances, and the purposes of Part 5.3A of the Act, I am satisfied entry into the Deed is contrary to the purposes of that Part of the Act. To allow the Deed to continue, in circumstances where there is no real prospect of the third defendant returning to trading, and where its continuation would result in the loss of the protection afforded to the plaintiff by the restraining order agreed to by consent, would amount to an abuse of the powers in Part 5.3A of the Act.
- [46] I am also satisfied the first and fourth defendants have used the powers under Part 5.3A of the Act in an attempt to avoid an investigation into past transactions, and to deprive the plaintiff of the protection afforded by the restraining order which they had only recently unsuccessfully attempted to vary.
- [47] The plaintiff has established that it is appropriate for the court to order that the operation of the Deed be terminated pursuant to s 447A of the Act.
- [48] The matters to which I have referred also satisfy me that there is otherwise good reason to terminate the Deed. It is in the interests of all creditors and members of the third defendant, including the plaintiff, that the operation of the third defendant be the subject of a full independent investigation. That is best achieved by the liquidation of the company.

- [49] Those findings render it unnecessary to determine the balance of the plaintiff's application. Had it been necessary, I would not have been satisfied the Deed ought to be terminated pursuant to s 445D(1)(a) of the Act.
- [50] Whilst the administrators' supplementary report to creditors, which was provided to creditors voting on the Deed, misstated the position of the plaintiff and his wife's employee entitlements, the misstatements were not so material as to have misled creditors.
- [51] My finding that the Deed should be terminated means the administrators' application must fail. The Deed is not a valid exercise of the powers of Part 5.3A of the Act. It should not be declared valid.
- [52] Further, I would not discharge the restraining order made by consent on 22 February 2012 so as to allow access to distribute those funds to unrelated creditors. Such an order would defeat the very purpose of that restraining order.
- [53] I shall hear the parties as to the form of orders, and costs.