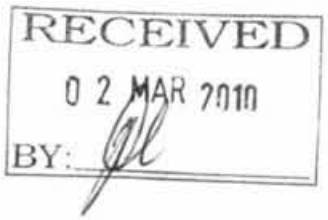
IPA

26 February 2010



The Hon James Wood AO QC
New South Wales Law Reform Commission
GPO Box 5199
SYDNEY NSW 2001

Dear Mr Wood

Security for costs and associated costs orders

We are responding to your letter of 11 December 2009 inviting the IPA to make a preliminary submission to this inquiry.

The Insolvency Practitioners Association (IPA) is the peak professional body representing company liquidators, trustees in bankruptcy, insolvency lawyers and other insolvency professionals, including financiers and academics. The IPA and its members necessarily have particular knowledge of and expertise in insolvency law and practice and the surrounding policies issues. We appreciate the opportunity to comment.

Summary

In making what is a preliminary submission, we give an outline of the law in relation to security for costs in so far as it relates to proceedings brought by registered liquidators and bankruptcy trustees, as plaintiffs. We do not raise any particular issues for reform or comment but do raise the question whether the issues that arise in relation to insolvency applications, in the context of security for costs, should have more specific rules that recognise the legal circumstances, terminology and the issues that arise in insolvency. If there are matters which you wish to follow up from this submission, we would be pleased to assist.

UCPR 42

In relation to UCPR 2005 42.21, we note that these particulars aspects relate to insolvency:

- (d) that there is reason to believe that a plaintiff, being a corporation, will be unable to pay the costs of the defendant if ordered to do so, or

- (e) that a plaintiff is suing, not for his or her own benefit, but for the benefit of some other person and there is reason to believe that the plaintiff will be unable to pay the costs of the defendant if ordered to do so,

Insolvency Practitioners Association of Australia ABN 28 002 472 362
33 Erskine Street, GPO Box 9985, Sydney NSW 2001 P+61 2 9290 5700 F +61 2 9290 2820 **www.ipaa.com.au**

- but that under sub rule (4), this "does not affect the provisions of any Act under which the court may require security for costs to be given".

Corporate insolvency

A plaintiff company may be a company in liquidation, administration or receivership.

Liquidators and administrators

Liquidators and administrators will typically bring many statutory recovery and other proceedings under the *Corporations Act* and at general law.

In the case of liquidation, some claims are required to be brought by the liquidator personally, others by the company in liquidation. The liquidator's general rights to sue 'in the name and on behalf of the company' are found in s 477(2)(a) and s 506(1)(b) of the *Corporations Act*. But proceedings in relation to voidable transactions under s 588FF(1) can only be made on the application of the liquidator, personally as the plaintiff.

In *Green* v *CGU Insurance Ltd*[1], the NSW Court of Appeal offered guidelines for courts considering applications for security for costs against liquidators, summarised in these terms:

- Liquidators suing personally are generally to be treated in the same way as natural persons. This means that costs orders will be made against them if proceedings fail (although with their right of indemnity against company assets) and security for costs may be ordered against them when the conditions set out in UCPR 42.21 are satisfied or (on appeal) there are 'special circumstances' within UCPR 51.50.
- Where the plaintiff is a company in liquidation and not the liquidator, then security for costs will more readily be ordered, against the company;
- Special considerations are said to apply where a litigation funder supports the liquidator and stands to make a commercial profit from success in the litigation. A court should be more ready to order security for costs where a person's interest is solely to make a profit from funding the litigation.

Generally, courts have to have regard to the danger that the court could be frustrating the liquidator in the exercise of her or his duties to recover assets on behalf of creditors, and to act in the public interest in bringing certain proceedings, if security were ordered.[2]

"suing, not for his or her own benefit"

We note that the UCPR refers to a plaintiff 'suing, not for his or her own benefit, but for the benefit of some other person'. While it has been said that this strictly applies to a liquidator suing for the benefit of others,[3] that is not of itself sufficient to justify security for costs in relation to a liquidator exercising a statutory right and duty to sue.

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[1] [2008] NSWCA 148; (2008) 67 ACSR 105; (2008) 26 ACLC 803

[2] See *Hall v Poolman* [2009] NSWCA 64. Liquidators may also be acting partly in their own interests, in recoupment of their remuneration and costs.

[3] See *Cowell* v *Taylor* (1885) 31 ChD 34 and *Re Strand Wood Co Ltd* [1904] 2 Ch 1.

Challenges to winding up orders

A company that challenges its own winding up order will normally be required to seek security for the costs of the appeal or challenge, which should be furnished otherwise than from the assets under the control of the liquidator: see *Tricorp Pty Ltd (in liq)* v DCT (1992) 10 ACLC 474.

Plaintiff in receivership

Where the plaintiff corporation is under the control of receivers and managers appointed by a secured creditor, and the proceedings are being conducted primarily for the benefit of that secured creditor, security may be ordered: see *Sent* v *Jet Corporation of Australia Pty Ltd* (1984) 2 FCR 201.

Plaintiff under Part 5.3A administration

The fact that the company is under Part 5.3A administration is no bar to an order for security for costs: *West's Process Engineering Pty Ltd* v *Westralian Sands & Anor* [1998] WASC 108; (1998) 16 ACLC 1,020. In such cases, the courts effectively treat the company as a solvent company, and apply the same discretionary considerations in relation to orders for security for costs. It may be otherwise if the administrator takes proceedings against a defendant that has allegedly acted to improve its position after the commencement of the administration, in breach of Pt 5.3A: *Timbertown Ltd v Holiday Coast Credit Union* (1997) 15 ACLC 1,679.

Personal insolvency

Trustees likewise bring proceedings for recovery of assets and under voidable transaction provisions under the *Bankruptcy Act*. They are then subject to costs orders against them personally, with a right of indemnity form the estate. The general rule is that the court does not require security for costs to be given by a plaintiff who sues as a trustee in bankruptcy even if there are no funds in the estate: see *Cowell v Taylor* (1885) 31 Ch D 34.

In cases where a bankrupt seeks to challenge the bankruptcy, by way of an annulment application or other means, no security is ordered, although the bankrupt can be subject to a costs order.

"... provisions of any Act under which the court may require security for costs .."

Section 1335 of the *Corporations Act* says that where a company is plaintiff the court may, if it appears that there is reason to believe that the company will be unable to pay defendant's costs, require security. Also, under s 462(4) of the Act, the court must not hear a winding up application by a contingent or prospective creditor unless and until security is given and a prima facie case for winding up the company has been established to the court's satisfaction.

The general power under section 30 of the *Bankruptcy Act* confers jurisdiction to award security for costs under which the Court would need to find that the order for security was "necessary for the purposes of carrying out or giving effect to the Act".

Preliminary comments

Liquidators and trustees bringing proceedings do so under duties to act with policy and other such considerations in mind that are different from normal commercial litigants. In particular, they are bringing proceedings on behalf of a necessarily insolvent entity, whose capacity to pay costs may be suspect; they do so on behalf of others, the creditors; and often with creditor or external funding. Their proceedings may be based on the public interest in upholding compliance with insolvency laws. That is not to say that security should not be ordered in appropriate cases, but that more particularly expressed rules be provided rather than the generically expressed terms of being 'unable to pay', and 'suing for the benefit of some other person', and the like; and with more particular criteria offered that are more apposite to those found in insolvency litigation.

If these comments raise issues for consideration, or if in the course of your inquiry you require further comment from us on these or other related issues, please contact me.

Yours sincerely

Michael Murray
Legal Director
Insolvency Practitioners Association

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