VOIDING TRANSFERS INTENDED TO DEFRAUD CREDITORS

Litigation Lawyers

INTRODUCTION

1. Section 228 of the *Property Law Act* enables a creditor to obtain an Order from the Court voiding a transfer which is intended to defraud creditors.

2. Section 228 provides:

> ***"228 Voluntary conveyances to defraud creditors voidable***
>
> *(1) Subject to this section, every alienation of property, made whether before or after the commencement of this Act, with intent to defraud creditors, shall be voidable, at the instance of any person prejudiced by the alienation of property.*
>
> *(2) This section does not affect the law of bankruptcy for the time being in force.*
>
> *(3) This section does not extend to any estate or interest in property conveyed for valuable consideration and in good faith to any person not having, at the time of the conveyance, notice of the intent to defraud creditors."*

3. There are similar sections in the other states and territories namely:

- ACT - S.239 of the *Civil Law (Property) Act 2006*;
- NSW – S. 37A of the *Conveyancing Act*;
- VIC – S. 172 of the *Property Law Act 1958*;
- SA – S. 86 of the *Law of Property Act 1936*;
- WA – S. 89 of the *Property Law Act 1969*; and
- NT – S. 208 of the *Law of Property Act*.

HISTORICAL BACKGROUND

4. The historical background to these sections was discussed in the case of *R v Dunwoody* [2004] QCA413. In that case as a McPherson J stated:

> *"[104] It is part of the ordinary processes of law that a judgment creditor may enforce his judgment by levying execution on land or other assets of the judgment debtor. Transferring those assets away from the judgment debtor in anticipation of such a judgment is designed to frustrate that process. Such conduct, whether or not it constitutes a crime or a "fraud" in the technical sense has long been the subject of statutory provisions avoiding that consequence. The Fraudulent Conveyances Act 1571; 13 Eliz, c 5, was by no means the first of its kind. The earliest was 50 Edw 3, c 6, passed in 1376, which recites and condemns the practice, said to be prevalent then, of secretly transferring one's tenements and chattels into the name of another and proceeding to live on the proceeds, so frustrating the efforts of execution creditors to obtain payment of their debts. It is precisely what the appellant had in mind here.*

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> *[105] The short title of that ancient statute of 1371 was "Fraudulent assurances of land or goods to*
> *deceive creditors, shall be void". The legislative remedy afforded was to authorise creditors to levy execution against such tenements and chattels "as if no gift had been made". The Statute of Elizabeth of 1571 recited a similar purpose, if with much less brevity. It is legislation that has been received or re-enacted in almost every place where English law now prevails. In this State, the local analogue is now to be found in* ***s 228(1)*** *of the Property Law Act 1974, and was formerly in s 46 of The Mercantile Act of 1867. Such statutory provisions operate independently of and beyond the limits of various provisions of the Bankruptcy Act 1966 which themselves have a common genesis in 13 Eliz 1, cap 5, or its forebears. See "Avoiding Transactions in Insolvency" in Corporate Insolvency Law, at 186-194 (ed Lessing & Corkery); Bond University 1995. Adjudication or sequestration in bankruptcy is not an element or a prerequisite of its application even though the official receiver or a trustee in bankruptcy may take advantage of it: Williams v Lloyd [1934] HCA 1; (1934) 50 CLR 341, 362-363.*
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> *[106] It is true that statutory enactments of this kind consistently refer to defrauding or deceiving "creditors"; but the course of judicial decision over the centuries shows that this expression is not to be confined to its limited and technical sense of a person to whom a debt is presently due and owing. May, on Fraudulent and Voluntary Dispositions of Property (3rd ed, 1980), at pp 43, 102, cites a body of judicial authority beginning with Twyne's Case [1601] EngR 4; (1602) 3 Co Rep 80b, at 81b; [1601] EngR 4; 76 ER 809, 816, in support of the proposition that the expression "creditors and others" in the old Elizabethan statute are "wide enough to include any person who has a legal or equitable right or claim against the grantor or settlor by virtue of which he is or may be entitled to rank as a creditor of the latter". He goes on to say that the claimant may be considered to be a creditor within the Statute although his claim had not become payable at the time when the conveyance was made and even though it was then merely contingent; and although it was a claim for unliquidated damages in respect of which judgment had not yet been given. Among the authorities cited is Barling v Bishopp [1860] EngR 934; (1860) 29 Beav 417; 54 ER 689, in which Romilly MR set aside a defendant's transfer of his land to his daughter after receiving notice of trial in an action for damages for trespass against him, in which the plaintiff obtained a verdict and judgment some two months later. Like the appellant here the defendant there subsequently sought and obtained relief in insolvency. Lord Romilly said [1860] EngR 934; (29 Beav 417, 420-421; [1860] EngR 934; 54 ER 689, 690) that "the only thing the Court has to consider is whether the object was to defeat the creditors present or in futuro".*
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> *[107] The provision in s 228(1) of the Property Law Act 1974 does not, like 13 Eliz, c 5, speak of creditors "or others". Having regard, however, to its history, I have little doubt that it would receive an interpretation that applied it to dispositions with intent to defeat a person with a claim that at the time of the disposition was still contingent or prospective, even one consisting as in Barling v Bishopp of unliquidated damages for a tort. But it is not necessary to decide that question now."* (emphasis added)

Accordingly it can be seen that the modern version of the enactment can be traced back to 1376.

ELEMENTS OF THE CAUSE OF ACTION

5. Clearly to be successful in such a claim it will need to be demonstrated that:

   (a) The plaintiff is a creditor;

   (b) There has been a transfer; and

   (c) The transfer was fraudulently intended to defeat creditors.

CREDITOR

6. There can be a current creditor or a prospective or contingent creditor.

7. In relation to this, in *Nelson v Mathai & Ors* [2011] FMCA 686 the Court stated:

> *"[9] In Barton v Deputy Federal Commissioner of Taxation [1974] HCA 43; (1974) 131 CLR 370 at 374 ('Barton') Stephen J said at paragraph [7]:*

> *This awareness of an impending liability is sufficient for the purposes of s. 40 (1)(c) [of the Bankruptcy Act 1996]. That paragraph employs language very similar to the reference, in the Statute 13 Eliz. c.5, to conveyances made "with intent to defraud, defeat or delay creditors" and it is well established that conveyances may fall within that Statute, although there existed no creditors at the date of conveyance, so long as the intent to defeat future creditors be made out - Mackay v. Douglas (1872) LR 14 Eq 106 ; Re Mackay (1951) 16 ABC 18, at p 28 . In Ex parte Russell (1882) 19 Ch D 588 , in which Sir Richard Malins' decision in Mackay v. Douglas (1872) LR 14 Eq 106 was applied, the members of the Court of Appeal again referred to the Statute of Elizabeth as concerned with the protection of future creditors. In Williams v. Lloyd [1934] HCA 1; (1934) 50 CLR 341, although the majority allowed the appeal, all the members of the Court treated the "intent to defraud creditors" to which s. 37A of the Conveyancing Act 1919 (N.S.W.) referred as capable of being established despite undoubted solvency at the time of the challenged alienation of property (1934) 50 CLR, at pp 360-361, 372, 377. So too in the case of s. 40 (1)(c) there may, I think, be the requisite intent despite the absence of existing indebtedness. A fortiori, the intent may exist if the debtor, unaware of his existing indebtedness, nevertheless believes in some impending indebtedness. Moreover an intent formed in relation to only one such existing or anticipated creditor will suffice, the combined effect of s. 23 (b) of the Acts Interpretation Act (Cth) and of s. 6 of the Bankruptcy Act producing this result. (at p374")"* (emphasis added)

8. In *Cannane v J Cannane Pty Ltd (In Liquidation)* [1998] HCA 26, Brennan CJ and McHugh J at paragraph [10] stated:

> *"The critical term for present purposes is "with intent to defraud creditors". Provisions of this kind, based on 13 Eliz I c 5, have been considered by the courts in various jurisdictions and it is clearly established that the party seeking to avoid a disposition of property has the onus of proving an actual intent by the disponor at the time of the disposition to defraud creditors. The creditors whom the fraudulent disponor of property might intend to defeat need not be existing creditors; they may be future creditors. The intent prescribed by s 121(1) is an intent to defraud any present or future creditors."* (emphasis added)

9. Holmes J of the Supreme Court in Queensland in *R v Dunwoody* [2004] QCA 413 cited Barton when her Honour stated at paragraph [119]:

> *"The expression "intent to defraud creditors", as used in s 121(1) before its amendment, was given a wide compass, extending to embrace an intention to defeat not merely existing creditors, but also future creditors: see Barton v Deputy Commissioner of Taxation of the Commonwealth of Australia*." (emphasis added)

10. In *PT Garuda Indonesia Ltd v Grellman* (1992) 35 FCR 515 at 523, the Court cited with approval (at 515) the following passage from Lewis' Australian Bankruptcy Law:

> *"The general principle may be stated that any dealing with property (other than by sale for a reasonable price) made with the object of putting it beyond the reach of present or future creditors comes within the definition of a fraudulent conveyance if the person concerned cannot immediately pay his debts or anticipates some event which may render him unable to pay his debts in future; such a dealing will be treated as fraudulent irrespective of the presence or absence of a conscious fraudulent intent on the part of the debtor if the necessary result of the dealing is to put the property beyond the reach of his creditors .... The word 'fraudulent' indeed has received an interpretation in bankruptcy matters somewhat wider than its ordinary use, and it may be defined as equivalent to 'with an intention to deprive creditors of recourse against all or any of his assets'."* (emphasis added)

TRANSFER OR DISPOSITION

11. Normally the existence of a transfer will be clear.

12. However, the type of transfer that is covered also includes, for example, the granting of a mortgage.

INTENT TO DEFRAUD CREDITORS

13. The section was discussed in *Williamson & McGillivray & Ors v JIA Holdings & Anor* [2011] QCA 346 as follows:

> *"[64] The operation of a section identical to s 228 was explained by Brennan CJ and McHugh J in DM Cannane and Anor v J Cannane Pty Ltd (In Liquidation) [1998] HCA 26; (1998) 192 CLR 557 (at 566-7):*

"But when the creditors ... intervene and the disposition is avoided, the property fraudulently disposed of becomes available for distribution among the then existing general body of creditors".

Although the party impugning the disposition of property must show an actual intent to defraud creditors at the time of the disposition, the intent may be inferred in the making of a disposition which, to adopt the words of Lord Hatherly LC in Freeman v Pope 'subtracts from the property which is the proper fund for the payment of [the] debts, an amount without which the debts cannot be paid'. The 'proper fund' may consist in assets out of which future creditors as well as present creditors would be entitled to be paid a dividend in respect of what is owing to them. Therefore a subtraction of assets which, but for the impugned disposition, would be available to meet the claims of present and future creditors is material from which an inference of intent to defraud those creditors might be drawn. Whether that inference should be drawn depends upon all the circumstances of the case." (footnotes omitted)

[65] That available assets are reduced as a result of the disposition of property can itself be a significant fact supporting the inference that the disposition was made with intent to defraud creditors. The effect of the cases was discussed by the Full Federal Court (Wilcox, Gummow and Von Doussa JJ) in P T Garuda Indonesia Ltd v Grellman (1992) 35 FCR 515 at 523-5:

"There is a substantial body of authority in decisions upon the Elizabethan Statute and its modern representatives which supports the statement by Clyne J in Re Trautwein ... :

> *'... it is ...clearly established that in determining whether or not an alienation has been made with intent to defraud creditors, a court must look at all the circumstances surrounding the alienation to ascertain if there were any such intent. It is not necessary to bring actual proof that the alienor had in his mind an intention to defraud creditors: for if it appears from the evidence that the effect might be expected to be and has in fact been to do so, the court will attribute the fraudulent intention to the alienor.'*

We refer to Freeman v Pope (1870) 5 Ch App 538 at 541 ... ; Mackay v Douglas (1872) LR 14 Eq 106 at 120 ... ; Re Simms [1930] 2 Ch 22 at 31-34 ... . Further, in this Court, the matter was discussed in detail in ... Noakes v J Harvy Holmes & Son (1979) 37 FLR 5. In the course of his judgment, with which Deane J and Fisher J agreed, Brennan J said (at 10-11):

> *'We were pressed with some observations in Williams v Lloyd; Re Williams where the court affirmed that the burden of proof that a transfer was made with a real intent to defeat or delay creditors is upon the party who so alleges. But that was a case where, at the time of the challenged disposition of property by a husband to his wife, he was in a sound financial position ... . In the present case, the inevitable result of the transfer ... was to defeat or delay any attempt to execute the judgment ... . The case falls squarely within the line of authorities of which Freeman v Pope is the leading example, where Lord Hatherley LC said (at 541):*
>
> *'But it is established by the authorities that in the absence of any such direct proof of intention, if a person owing debts makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid, then, since it is the necessary consequence of the settlement ... some creditors must remain unpaid, it would be the duty of the judge to direct the jury that they must infer the intent of the settlor to have been to defeat or delay his creditors... .'*

That proposition does not trespass upon the rule as to onus of proof; it is a particular illustration of the discharge of the onus by inference from the known facts.'" (footnotes omitted)

[66] Garuda was referred to by Brennan CJ and McHugh J in their judgment in Cannane. Their Honours did not expressly endorse the passages I have quoted but the case was referred to without dissent or criticism. As well, their Honours quoted with approval a part of Lord Hatherley's judgment which was quoted at greater length by the Full Federal Court. The judgments in Cannane do not, I think, cast any doubt upon what was said in Garuda and Trautwein. Clyne J did not say that a subjective intention to defraud did not have to be proved. The passage in Trautwein says that if a disposition of property had the result that creditors would not be paid, and viewed objectively those disposing of the property "might be expected to" understand that would be the effect, the court will infer the actual intent to defraud."

14. In *Ivanovski v Keith Stevens McConnell as representative of the estate of Walter Perdacher (deceased)* [2009] NSWSC 1036, the court stated:

> *[73] Whether the alienation was made with intent to defraud creditors as contemplated by* ***s 228****(1) of the Act is a question of fact and the onus of establishing the fact is on the plaintiffs.*

[74] The intention to defraud may be established and inferred from the surrounding circumstances. Each case must be considered as a matter of fact on its own facts: Williams v Lloyd [1934] HCA 1; (1934) 50 CLR 341; World Expo Park Pty Ltd v EFG Australia Ltd (1995) 129 ALR 685 at 701; D M Cannane & Anor v J Cannane Pty Limited (In Liq) & Anor [1998] HCA 26; (1998) 192 CLR 557 at 566.

[75] It is not necessary for the plaintiff to prove that Walter actually had in his mind an intention to defraud creditors. If it appears from evidence of all the circumstances that the transfer might be expected to have that effect, and has had that effect, the Court will attribute fraudulent intention to him: Re Trautwein; Richardson v Trautwein (1944) 14 ABC 61; P T Garuda Indonesia Ltd v Grellman (1992) 35 FCR 515 at 523-4; D M Cannane v J Cannane at 566.

[76] If the conveyance is voluntary it is easier to infer a dishonest intention than when it is made for consideration: Freeman v Pope (1875) LR5 Ch App 538.

[77] In Neat Holdings Pty Ltd v Karajan Holdings Pty Ltd [1992] HCA 66; (1992) 67 ALJR 170 at 170-1, Mason CJ and Brennan, Deane and Gaudron JJ said:

> *"The ordinary standard of proof required of a party who bears the onus in civil litigation in this country is proof on the balance of probabilities. That remains so even where the matter to be proved involves criminal conduct or fraud. On the other hand, the strength of the evidence necessary to establish a fact or facts on the balance of probabilities may vary according to the nature of what it is sought to prove. Thus, authoritative statements have often been made to the effect that clear or cogent or strict proof is necessary "where so serious a matter as fraud is to be found". Statements to that effect should not, however, be understood as directed to the standard of proof. Rather, they should be understood as merely reflecting a conventional perception that members of our society do not ordinarily engage in fraudulent or criminal conduct and a judicial approach that a court should not lightly make a finding that, on the balance of probabilities, a party to civil litigation has been guilty of such conduct. As Dixon J commented in Briginshaw v Briginshaw:*
>
> > *"The seriousness of an allegation made, the inherent unlikelihood of an occurrence of a given description, or the gravity of the consequences flowing from a particular finding are considerations which must affect the answer to the question whether the issue has been proved ..."*

15. As stated in the High Court decision in *Marcolongo v Chen* [2011] HCA 3, an intention to hinder or delay creditors is sufficient:

*[18] However, the better view of the abbreviated terms employed in s 172 and s 37A is that of Pennycuick V-C in Lloyds Bank Ltd v Marcan**[32]**. This is that, beginning with its appearance in the consolidation provision in the 1924 Act, the term "defraud" was designed to reproduce the meaning of the expression "delay, hinder or defraud" in the Elizabethan Statute. That statute was understood as if it read "delay, hinder or [otherwise] defraud". The contrary has not been suggested in the present case.*

*[19] From this legislative history two things of immediate relevance appear. The first is that an understanding of the issues in this appeal is assisted by consideration of the case law upon the Elizabethan Statute which had been built up before that statute's repeal and restatement in s 37A. The second is that, in accordance with that case law, exemplified by remarks of Lord Mansfield**[33]**, and more recently of Arden LJ**[34]**, the provision and its modern representatives should receive a liberal construction in effecting their purpose of suppressing fraud.*

and further:

*[32] However, …Mrs Marcolongo correctly relies upon a statement by Blanchard and Wilson JJ when considering the comparable New Zealand legislation**[65]** in Regal Castings Ltd v Lightbody**[66]**. Their Honours said that it was unnecessary to show that the debtor wanted creditors to suffer a loss or that the debtor had a purpose of causing loss: it was necessary to show the existence of an intention to hinder, delay or defeat creditors and in that sense to show that accordingly the debtor had acted dishonestly. Mrs Marcolongo correctly relies also upon the observation by Russell LJ when considering s 172 of the 1925 Act in Lloyds Bank Ltd v Marcan**[67]**. His Lordship said:*

> *"I am not sure what is meant by a perfectly innocent defeat, hindrance or delay. It must be remembered that in every case under this section the debtor has done something which in law he has power and is entitled to do: otherwise it would never reach the section. If he disposes of an asset which would be available to his creditors with the intention of prejudicing them by*

> *putting it, or its worth, beyond their reach, he is in the ordinary case acting in a fashion not honest in the context of the relationship of debtor and creditor. And in cases of voluntary disposition that intention may be inferred. ... The intention of Mr Marcan is perfectly plain: the lease to his wife was designed expressly to deprive the bank of the ability to obtain the vacant possession to which the bank plainly attributed value, and to diminish to that extent the strength of the bank's position as creditor. To take that action at that juncture, in my judgment, was, in the context of relationship of debtor and creditor, less than honest: it was sharp practice, and not the less so because he was advised that he had power to grant the lease. It was, in my judgment, a transaction made with intent to defraud the bank within section 172, and would have been within the [Elizabethan Statute]."*

*[33] To that may be added the statement in the joint reasons of the Court in Farah Constructions Pty Ltd v Say-Dee Pty Ltd**[68]**:*

> *"As a matter of ordinary understanding, and as reflected in the criminal law in Australia**[69]**, a person may have acted dishonestly, judged by the standards of ordinary, decent people, without appreciating that the act in question was dishonest by those standards. Further, as early as 1801, Sir William Grant MR stigmatised those who 'shut their eyes' against the receipt of unwelcome information**[70]**."*

*[34] Lym relied upon the references by Brennan CJ and McHugh J in Cannane v J Cannane Pty Ltd (In liq)**[71]** to "the onus of proving an actual intent". But their Honours were adding the word "actual" as a periphrasis to emphasise that, while the existence of the intent might be inferred from the evidence, it was to be found as a fact. With Gaudron J and Gummow J, Brennan CJ and McHugh J concluded that the facts of Cannane did not support the drawing of such an inference**[72]**.*

REMEDIES

16. The appropriate remedy was discussed in *Singh v Kaur Bal* [2011] QASC 303:

> *[72] In determining the appropriate remedy, the starting point is the language of s 89. The section renders alienations made with the proscribed intent 'voidable'. The concept of avoiding a transaction involves undoing or reversing the transaction. To my mind, a natural starting point when a transaction is found to be voidable under s 89is to reverse the transaction by ordering a retransfer to the alienating party, or by declaring a trust in favour of that party. The latter was the effect of the primary judge's order in Chen v Marcolongo [2009] NSWCA 326 [314]. Another order to substantially the same effect would be that the interest be held on trust for the transferor's creditors. That was the form of order contemplated by Pullin J in First Industry Corp v Goh [36].*
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> *[73] A claim under s 89 does not create any security interest over the property the subject of the alienation: Chen v Marcolongo [315]. Nor, in my opinion, does it create any priority for the debt owed to the plaintiff in the s 89 claim over other creditors of the alienating debtor. That seems to me to be consistent with the approach taken in Langdon v Gruber [2001] NSWSC 276 [79] [87], although a contrary approach appears to have been taken in Sanwa Home Australia Pty Ltd v Sanwa Home Inc (Unreported, QSC, No 942 of 1994, 14 September 1995).*

17. As quotes above, the NSW first instance decision in Chen at [315]:

> *"The mere fact that she has made a claim which is before the District Court and may be entitled to apply under **s 37A** of the Conveyancing Act 1919 does not give her any more security than a Mareva injunction would. In other words, no security."*

18. A number of cases also involve. In an interim basis, a Mareva Injunction.

GENERAL POINTS

19. Many of the cases discuss the rule in *Jones v Dunkel*. It can be seen that the person who will know about the transaction under attack will be the defendant, and therefore, failure by the defendant to provide explanation will raise the potential for such inference to be relied upon by the Plaintiff.

Malcolm Robinson