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WINDING UP BY THE COURT FOR INABILITY TO PAY DEBTS: THE COURT'S EXERCISE OF ITS DISCRETION

The inability of companies to pay their debts — ie insolvency — is the most frequently-used ground for the compulsory winding up of companies. This ground, s 364(1)(e) of the National Companies Act 1981 (herein NCA) [s 222(1)(e) of the Companies Act 1962-1980 (SA) (herein UCA)] is regularly before the courts, more so in recent years. This article discusses s 364(1)(e) and s 364(2) and their predecessors in an attempt to highlight trends and problems in their application. The court has under s 364(1) a discretion whether or not to wind up a company. Thus one must bear in mind that cases about the exercise of discretion are, as Harman LJ has put it, "no more than guides or signposts along the road..." [1] Even where the threshold requirements of the statute are met it is possible that the court may not order a winding up. But this is an area of practical importance, where judicial decisions have profound effects on individual companies, their associated companies, contributories, creditors and employees. Such are the consequences that the court in exercising its discretion must be guided by clear and fair principles, and it must apply them consistently, even though decisions are made under pressure of time during often crowded motions and petitions days. This article examines both the statutory procedures and the exercise of the court's discretion in creditors' winding up proceedings.

The Statutory Grounds for Winding Up for Insolvency

Section 364(2) [s 222(2) UCA] offers a petitioner or an applicant (as he is called in the NCA) three possible ways of statutorily proving a company is unable to pay its debts for the purposes of s 364(1)(e) [s 222(1)(e) UCA].

"SECTION 364: CIRCUMSTANCES IN WHICH COMPANY MAY BE WOUND UP BY COURT

364(1) [Circumstances] The Court may order the winding up of a company if — ...

(e) the company is unable to pay its debts;...

364(2) [Deemed insolvency] For the purposes of sub-section (1), if —

(a) a creditor by assignment or otherwise to whom the company is indebted in a sum exceeding $1,000 then due has served on the company a demand, signed by or on behalf of the creditor, requiring the company to pay the sum so due and the company has, for 3 weeks after the service of the demand, failed to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor;

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1 In *Re LHF Wools Ltd* [1970] Ch 27, 36; citing Upjohn LJ in *Re P & J Macrae Ltd* [1961] 1 WLR 229, 237.

(b) execution or other process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or

(c) the Court, after taking into account any contingent and prospective liabilities of the company, is satisfied that the company is unable to pay its debts,

the company shall be deemed to be unable to pay its debts."

Section 364(2)(a) is the most frequently used, but any one or a combination of them may be relied on in winding up proceedings. Paragraph (b) has not been controversial. Paragraph (c) is often used as a backstop to paragraph (a). They may both be listed in the applicant's pleadings and if some defect invalidates paragraph (a), paragraph (c) – which requires no notice procedure – may remain as an alternative. The latter is suitable for speedy proceedings when a demand has not been made, or where a company by special resolution determines to be wound up by the court. Especially with smaller companies, s 248(4) NCA [s 144(2) UCA], which allows the waiving of notice for the meeting called to pass the special resolution, can shorten the process.[2]

Paragraph (c) simply requires the applicant to satisfy the court that the company is unable to pay its debts, and there is no $1,000 minimum requirement as there is with paragraph (a).[3] There appears to be an accepted, although not undisputed,[4] rule that only in special circumstances will the court grant a paragraph (b) or (c) based petition when the applicant's debt is less than $1,000: the special circumstances arise where the applicant's (ie petitioner's) application is supported by other creditors whose debts, added to that of the petitioner, total more than $1,000.[5]

What is the standard of proof of this inability to pay debts? A casual approach is inappropriate; something more than a mere admission or

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2 However, a winding up by the court is not necessarily either quicker or more economical than a members' voluntary winding up. See *Re Southard & Co Ltd* [1979] 1 WLR 1198, 1206 per Buckley LJ.

3 See *Re Metropolitan Fuel Pty Ltd* [1969] VR 328, 329 per Pape J: "It is clear that, since the petitioning creditor is not relying upon the special provision in s.222(2)(a), in order to establish that the company is unable to pay its debts, she may petition to wind the company up even if her debt was found to be less than £50: see *Re Yate Collieries & Limeworks Co.* [1883] W.N. 171; *Re Alderney Dairy Co. Ltd.* (1885), 11 V.L.R. 628; *Palmer,* 17th ed, vol.2, pp.25, 26."

4 See *Palmer's Company Precedents*; Part 2; *Winding-Up Forms & Practice* (17th edn 1960) 26.

5 *Re Metropolitan Fuel Pty Ltd* [1969] VR 328, 329. In a recent dictum Slade J in *Re Capital Annuities Ltd* [1978] 3 All ER 704, 718 purported to add a gloss to the words of the statute:

> "I cannot, however, accept that mere evidence that a company...has for the time being insufficient liquid assets to pay all its presently owing debts, *whether or not repayment of such debts has been demanded,* by itself proves inability on its part to pay its debts, within the meaning of ss.222 and 223 of the 1948 Act..." [UCA, ss221 and 222].

He implies that some sort of demand is required before liabilities are taken into account and compared with available assets to prove inability to pay, although it is not specifically asked for except under paragraph (a). He did add however that the figures put to him were up to three years old and thus insufficient proof of the company's inability to pay. The court, he said, requires up to date, although not necessarily formal, valuations of the company's liabilities and assets.

allegation of insolvency is needed. In *Re Exclusive Master Book-Binding & Manufacturing Co Pty Ltd,*[6] for example, Bray CJ stressed that s 222(2)(c) [s 364(2)(c) NCA], unlike the previous two paragraphs (where service and non-compliance created the presumption of inability to pay debts), required positive evidence of the company's inability. The third paragraph or ground "is not proved simply by the allegation that the company is unable to pay its debts, because the court has to be satisfied that that is so".[7] The court seeks this proof in the affidavits and oral evidence presented by the applicant: large bank overdrafts, dishonoured cheques, unpaid bills, unpaid wages, unsatisfied judgments against the company are indicia of insolvency. A simple admission by the company's counsel that the company is insolvent and wishes to be wound up is insufficient.[8] No matter whether the company itself or some creditor is seeking a winding up for insolvency the rule is the same — a mere allegation or statement of insolvency is insufficient.[9]

If paragraph (c) is used the Court *must* consider the "contingent and prospective" liabilities of the company when determining whether a company is unable to pay its debts. A surety is an example of a contingent creditor: a debt will only become due on an event that may or may not occur. A loan payable on demand which is not immediately payable, because not yet demanded, is an example of a prospective liability. Contingent and prospective liabilities are familiar in the insurance industry where liability may or will arise on the occurrence of future events or at some future date.[10]

Does inability to pay debts mean inability to meet current demands; or does it mean that the company's assets are exceeded by its liabilities? The court and textwriters have coined the phrase "commercial insolvency" to describe the former. Insolvency in winding up hearings is widely acknowledged as the "inability to pay debts as they fall due and not a deficiency of assets as compared with liabilities."[11] Thus a company may

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6 [1977] ACLC 29,572, 29,575.

7 Ibid 29,575. See also Slade J in *Re Capital Annuities Ltd* [1978] 3 All ER 704, 718-719. The petitioner in *Re Gold Hill Mines* (1882) 23 Ch D 210, 214 was roundly condemned by Jessel MR: "There is not a particle of evidence in support of this allegation. He cannot allege a single circumstance to shew insolvency, but he relies on the general allegation of insolvency contained in his own affidavit in support of the petition." See also *Re Milo Wheat Co Ltd* [1925] 2 DLR 1170, 1175-1176.

8 *Re Grundy Stove Co* (1904) 7 OLR 252.

9 As, eg, in *Re Accord Pty Ltd* [1977] ACLC 29,417.

10 Such contingent liabilities were unsuccessfully relied on in a paragraph (c) based petition in *Re Capital Annuities Ltd* [1978] 3 All ER 704. In *Stonegate Securities Ltd* v *Gregory* [1980] Ch 576, 579 Buckley LJ defines contingent and prospective creditors. See also Pennycuick J in *Re William Hockley Ltd* [1962] 2 All ER 111, 113; Matthews J in *Re Community Development Pty Ltd* [1968] Qd R 548, 552.

11 *Mann* v *Goldstein* [1968] 2 All ER 769, 778 per Ungoed-Thomas J; see also Bray CJ in *Pizzey Ltd* v *Classic Toys Pty Ltd* [1975] ACLC 28,011, 28,015. Plowman J in *Re Tweeds Garages Ltd* [1962] 1 Ch 406, 410 cited *Buckley on the Companies Acts* (13th edn 1957) 460 which reads: "The particular indications of insolvency mentioned in paras (a), (b) and (c) [equivalent to UCA s 222(2)(a) and (b)] are all instances of commercial insolvency, that is of the company being unable to meet current demands upon it. In such a case it is useless to say that if its assets are realized there will be ample to pay twenty shillings in the pound: this is not the test. A company may be at the same time insolvent and wealthy. It may have wealth locked up in investments not presently realizable; but although this be so, yet if it have not assets available to meet its current liabilities it is commercially insolvent and may be wound up." Slade J in *Re Capital Annuities Ltd* [1978] 3 All ER 704, 718-719 also cited this passage from

be insolvent — commercially insolvent — even though its balance sheets show large surpluses of assets over liabilities. A temporary lack of liquidity is, however, unlikely to render a company insolvent.[12]

When paragraphs (a) and (b) of s 364(2) are relied on by the petitioner there are usually few problems — a company is "deemed" to be unable to pay its debts if some sort of demand for a current debt is not met. Though usually a more difficult task, under paragraph (c) it may be enough if the petitioner can show the company has insufficient "existing and probable" [13] assets to meet existing, contingent and prospective liabilities.

Procedural Requirements

The s 364(2)(a) or demand procedure offers a convenient method for determining statutory insolvency. It is only open to creditors to whom the company is presently indebted for $1,000 or more [$100 in the UCA]. Thus it is not available to contingent or prospective creditors.[14] The creditor serves a "demand" on the debtor company requiring it to pay the due amount. If the company after 3 weeks has "failed" ["neglected" in the UCA] to pay, the company is deemed insolvent. Accordingly a winding up petition may be filed and the court, at its discretion, may order that the company be wound up.

The court demands exact compliance with the demand procedure set out in paragraph (a). It insists there be a genuine creditor, an established debt, and proper compliance with the notice and service requirements of the Act. While the applicant must meet strict standards, the company has slightly more leeway. Gibbs J in *Re QBS Pty Ltd* [15] held that on a proper construction of s 222(2)(a) UCA — notably of the use of the present tense of the verb "is indebted" — the company cannot be deemed unable to pay its debts if the debt is paid at least *before the petition is presented.* Failure to comply within the three weeks demand period is not necessarily fatal for the company. Gibbs J left open the question whether this latitude could extend beyond presentation. If one accepts a company should have every chance to remain in existence and that the creditor's sole interest is to get paid, there seems little reason for not extending the

11 *Cont.*
Buckley. Recently Buckley LJ in *Stonegate Securities Ltd* v *Gregory* [1980] Ch 576, 584 defined "commercial solvency" of a company as being "its ability to pay its debts as they fall due". See also McPherson, *The Law of Company Liquidation* (2nd edn 1980) 44: cf 48-49.

12 Barwick CJ in *Sandell* v *Porter* (1966) 115 CLR 666, 670, discussing what is now s 122(1) of the Bankruptcy Act 1966 concluded: "It is the debtor's inability, utilizing such cash resources as he has or can command through the use of his assets, to meet his debts as they fall due which indicates insolvency." He thought that one should take into account "moneys which he [the debtor] can procure by realization by sale or by mortgage or pledge of his assets within a relatively short time — relative to the nature and amount of the debts and to the circumstances, including the nature of the business, of the debtor." Also see McDonald, Henry & Meek, *Australian Bankruptcy Law and Practice* (5th edn 1977) para 686.

13 See *Buckley on the Companies Acts* (13th edn 1957) 460.

14 See Buckley LJ in *Stonegate Securities Ltd* v *Gregory* [1980] Ch 576, 579-581.

15 [1967] Qd R 218, 223-224.

latitude until the hearing of the application[16] or even until a winding up order is actually handed down. An analogy can be drawn with the right of the mortgagor to redeem his property by paying the mortgage debt up until the property is actually sold by or on behalf of the mortgagee.

Once the order is pronounced, but in the intervening period before it is drawn up, can the company halt the winding up by paying off its debts? The court will allow this, although a company's application for rescission of an order must be supported by the creditor, and by a favourable affidavit setting out the company's assets and liabilities.[17] The judge or Master who pronounced the order may recall it on his own initiative too.[18]

While the convenience of the demand procedure is undoubted, the creditor must take pains entirely to comply with the requirements. In *Re Willes Trading* [19] for example, the petition was dismissed simply because it had been addressed to "Willis Trading" and not to "Willes Trading".

A full three weeks must also lapse from the time of service of the demand to the time of presentation of the application. Megarry J in *Re Lympne Investments Ltd* [20] dismissed a petition because it was presented one day too soon. The demand was served on the company on 4 November and the petition was presented at midday on 25 November. Megarry J insisted that "the normal rule for the computation of time" be observed: [21] that is, the day of service and fractions of days are excluded where the period of time is expressed in days or longer units of time. Section 26(1) of the Companies and Securities (Interpretation and Miscellaneous Provisions) Act 1980, under which time is normally to be reckoned exclusive of the day of service, takes care of this matter for the future.

While no special form is required, the creditor's demand must be a demand, not merely a certificate or statement of debt.[22] And under

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16 See *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,643 per McGarvie J. Recently in *Re a Company* (1980) 35 ACTR 36 Kelly J held that where the petitioner's debt (plus costs) had been repaid a petitioner could withdraw a petition after presentation and before advertisement. Because it in effect invites other creditors or contributories to become parties, advertisement is of major significance.

17 See *Gore-Browne on Companies* (42nd edn 1972, eds Boyle and Sykes) 929, esp n 244. Note particularly two *Practice Notes* on this matter in [1971] 1 WLR 4 and 757. The English Companies Court grants rescission of winding up orders until they have been perfected or drawn up. Pennycuick VC in the second *Practice Note* pointed out that the costs of unsuccessful applications usually fall on the creditor (or contributory) making or joining in the application. If in these rescissions the costs fall on the company, they will fall unfairly on the general body of creditors. Thus such applications, Pennycuick VC noted, would only be entertained if made by a creditor (or contributory), or by the company jointly with the creditor (or contributory). See also 7 *Halsbury's Laws of England* (4th edn) p 622, para 1042. In *Re XL Petroleum Ltd* [1971] ACLC 27,173 Gillard J recalled an order pronounced some three days earlier but which had not yet been passed and entered. He noted that "this is a power that should be sparingly exercised", but which could be exercised "where an injustice might be done if the order for winding up were allowed to stand, and where, on the other hand, no injustice would be done to anybody if it were recalled." (27,176).

18 *Re XL Petroleum Ltd* [1971] ACLC 27,173, 27,176.

19 (1978) 3 ACLR 582; [1978] ACLC 30,065.

20 [1972] 2 All ER 385.

21 Ibid 387-388. See also *Palmer's Company Law* (22nd edn 1976) vol 1, 886; *Re North, ex parte Hasluck* [1895] 2 QB 264.

22 *Re No 82 Garden Units Pty Ltd* [1965] NSWR 1452.

s 528(1) NCA the notice of demand should be left at (or sent to) the registered office of the debtor company,[23] not at some other place that may seem even more appropriate, such as the office of its accountant as in *Re Mannum Haulage Pty Ltd.*[24] Section 217 [s 112 UCA] requires notice of the address of a company's registered office and of any change to that address to be lodged with the Commission. Section 528(2) NCA deems the registered office of the company to be that which has been lodged with the Commission under s 217 NCA. This answers the problem that arose in *Re Alpina Pty Ltd* [25] where a notice of demand was left at the address that had been notified to the Registrar and not at the actual office at a new address.

A recent decision draws attention to the need for careful drafting of winding up applications too. In *Kevalair Pty Ltd* [26] Needham J rejected a petition and refused to allow amendment of the pleadings. The petition, he said,

> "lacks particularity; it makes unparticularised allegations of fraud; and it alleges the entitlement of the petitioners to be registered as shareholders by virtue of what appear to be contradictory entitlements. Further, there are a number of provisions in the petition which are practically incomprehensible." [27]

His Honour was encouraged in his outright rejection of the petition by the fact that a winding up would be deemed under s 223(2) UCA to have commenced retrospectively from the date of presentation of the petition. This of course would adversely affect the company's affairs from that date. This ill-drafted petition he thought to be unworthy of this effect.

On occasion the court has been less than unyielding over procedural requirements. For example, in *Re Leonard Spencer Pty Ltd*[28] the petitioner breached the then equivalent of r 48 of the Rules of Court (Companies Act) 1965 (SA) which provided that a petition should be advertised not later than seven days after its presentation. The petition was advertised 12 days from presentation. However Gibbs J simply ruled that "no substantial injustice has been caused, and, under s. 374, I declare that the proceedings are valid notwithstanding the irregularity." [29] Section 539(2) [s 366(1) UCA], which permits the court to overlook "irregularity or deficiency of notice or time", arguably could apply in the *Re Mannum Haulage Pty Ltd* situation. But Walters J, deriving support from old English cases, felt unable to apply the section there. Section 222(2)(a) [now s 364(2)(a)], he said, should be followed and its wording was clear.

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23 This specific requirement does not appear in s 364(2)(a) NCA as it did in s 222(2)(a) UCA. However s 528 NCA (like s 362 UCA) preserves the requirement, although service at the registered office is mandatory under s 222(2)(a); it is not under s 528(1) NCA.

24 (1974) 8 SASR 451. See also *Re GT Motor Inns Pty Ltd*, unreported, NSW Supreme Ct (19 May 1980).

25 [1977] 74 LSJS (SA) 117. Hogarth J's call (at 120) for greater particularity in registered office addresses is met by s 217(1) NCA.

26 [1980] ACLC 34,189.

27 Ibid 34,193.

28 [1963] Qd R 230.

29 Ibid 237.

It is noteworthy that s 364(2)(a) NCA substitutes the words "failed to pay" for the old formula, "neglected to pay". The latter at first blush seems merely a rather quaint and tactful way of saying the former. Megarry J inclined to this view:

> "If there is liability, a failure to discharge that liability may well be 'neglect' whether it is due to inadvertence or obstinacy or dilatoriness..." [30]

Furthermore, the rewording seems clearer. The debtor must "fail" to pay within the allotted time. Whether it is termed "neglect" or "failure" is of scant concern one might think.

It is interesting, though, to consider the words of Jessel MR in *Re London and Paris Banking Corporation,*[31] one of the seminal decisions establishing the bona fide dispute test for insolvency cases. He distinguished "neglected" from "omitted". And "omitted" is a much closer synonym for "failed" than is "neglected".

> "It is very obvious, on reading that enactment [1862 UK Act], that the word 'neglected' is not necessarily equivalent to the word 'omitted'. Negligence is a term which is well known to the law. Negligence in paying a debt on demand, as I understand it, is *omitting to pay without reasonable excuse. Mere omission by itself does not amount to negligence.* Therefore I should hold, upon the words of the statute, that where a debt is *bona fide* disputed by the debtor, and the debtor alleges, for example, that the demand for goods sold and delivered is excessive, and says that he, the debtor, is willing to pay such sum as he is either advised by competent valuers to pay, or as he himself considers a fair sum for the goods, then in that case *he has not neglected to pay, and is not within the wording of the statute."*[32] [Emphasis added].

The Master of the Rolls based his application of the bona fide dispute test (discussed later) directly on the word "neglected". Alternative wording — "omitted" or "failed" — does not carry the same connotation. Refusing to pay a disputed debt is still "failure" to pay, whereas (adopting Jessel MR's interpretation) it may not be "neglecting" to pay. In ordinary usage "neglected" means more than "omitted" or "failed".

Echoes of Jessel MR's statement can still be heard today. McGarvie J in *Fortuna Holdings Pty Ltd* v *Federal Commissioner of Taxation* noted:

> "It is established that non-compliance with a demand for payment does not amount to neglect within sec 222(2)(a) of the *Companies Act* where the existence of the debt is genuinely disputed by the company on substantial grounds..."[33]

So too in *Re Jeff Reid Pty Ltd* McLelland J relied specifically on *Re London and Paris Banking Corp* when he noted: "Mere omission to pay

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30 *Re Lympne Investments Ltd* [1972] 2 All ER 385, 389.
31 (1874) 19 LR Eq 444.
32 Ibid 446.
33 [1976] ACLC 28,634, 28,648.

a debt on demand does not of itself constitute "neglect" to do so within the meaning of sec 222(2)(a)..." [34]

Can the court invest the word "failed" in s 364(2)(a) with the same meaning? Jessel MR's reliance on a rather narrow interpretation of "neglected" and the concept of negligence as the basis on which a successful dispute could be founded suggests it should not. Can it then be argued that in choosing the word "failed" in place of "neglected" the legislature is deliberately removing the substantial dispute defence to creditor's applications? This seems most unlikely. The word "fails" has received flexible interpretation in the context of other statutes.[35] And failing to pay because one has a reasonable or substantial excuse or dispute is surely not failing to pay within the meaning of the new section. Furthermore can you fail to pay someone whose status as a creditor is, by the established criteria, not adequately established? Any applicant whose entire "debt" is subject to substantial dispute has neither a debt nor standing as a creditor. A company cannot "fail" or "neglect" to pay such a disputed "debt".

Locus Standi under s 364(2) [s 222(2) UCA]

The question of locus standi in winding up proceedings is often a vexed one for putative creditors. The courts insist that persons presenting applications as creditors must in fact be creditors, ie that their debts be established beyond substantial dispute.

Under s 363 [s 221 UCA] a creditor includes both the creditor to whom the money is presently payable *and* "a contingent or prospective creditor". Section 363(3), though, forbids the Court to "hear" proceedings commenced by a contingent or prospective creditor until "a *prima facie* case for winding up has been established to the satisfaction of the Court." Such a case will not be established, it seems, if there is bona fide dispute over whether the company's debt is presently due or is prospective or contingent.[36]

Aside from the cross-claim cases, a company most frequently bases its request for restraint or dismissal of winding up proceedings on a dispute as to whether the alleged debt exists, and thus as to whether there is a creditor at all. As Ungoed-Thomas J noted in his influential judgment in *Mann* v *Goldstein:*

34 [1980] ACLC 34,330, 34,333. See *Dow Securities Pty Ltd* v *Manufacturing Investments Ltd* [1981] ACLC 33,173, 33,176. See also O'Bryan J, in *Re K L Tractors Ltd* [1954] VLR 505, 508-509: "The words..."neglected to pay the sum" might well have been interpreted as meaning no more than "omitted to pay" as like words of the English *Bankruptcy Act* 1869, sec 6, were interpreted...However, this is not so..."

35 See, for example, Nagle J's discussion of the word "fails" as used in s 223 of the Income Tax Assessment Act 1936 (as amended) in *Ganke* v *DFC of T* (1975) ATC 4,097, 4,101-4,102. He thought that, for example, connotations of "carelessness or delinquency" could be read into the word, depending on the context in which it is used.

36 See discussion on prospective and contingent creditors in *Stonegate Securities Ltd* v *Gregory* [1980] 1 Ch 576. See also text accompanying n 10 above, and brief discussion of *Re Laceward Ltd,* infra n 167.

> "Once it becomes clear [ie that there is no debt and thus no creditor], pursuit of the petition would be an abuse of process, and this court would restrain its presentation or advertisement." [37]

The courts vigorously condemn attempts to use the winding up threat to put pressure on companies where the debt is still a matter of substantial dispute. If the existence (as distinct from the quantum) of the specific debt is doubtful, then so too is the applicant's status as a creditor.[38]

In *Re Horizon Pacific Ltd* [39] Needham J applied himself to the question of standing:

> "When the issue is one of law, it is a matter for the Court to determine, in its discretion, whether it should decide the point in the petition or leave it to be decided in proceedings brought for that purpose. Where the question whether the petitioner is a creditor is dependent for its resolution upon issues of fact which are not conceded and need proof, prima facie, provided there is a dispute on substantial grounds as to the petitioner's status, the issues should be tried in the normal way." [40]

Questions of whether or not there is a creditor or a debt within the meaning of s 364 are rarely decided by the court hearing the winding up proceedings. In *Re Horizon Pacific Ltd*, for a typical example, the Court stayed the petition pending the outcome of proceedings to determine the existence of a debt. However, as noted by McGarvie J in *Fortuna Holdings Pty Ltd* v *Federal Commissioner of Taxation,*[41] Gibbs J in *Re QBS Pty Ltd,*[42] and Needham J in *Re Nickel Mines Ltd,*[43] there do arise special circumstances which justify the court deciding, where possible and convenient, on the existence of a debt in the winding up proceedings themselves: for example, if the court has before it all the evidence which is likely to be brought in separate proceedings to establish the debt.

Effects of presentation and advertisement of application

The court's sensitivity over lack of standing in applicants and the misuse of the winding up procedures is well-founded. Mere presentation of a winding up application can have profound ill-effects on a company. As required by Rules 17 and 48 of the Rules of Court (Companies Act) 1965-1980 (SA) and their equivalents elsewhere, the application or petition is gazetted and advertised to the public in a daily newspaper within 14 days of presentation to the court. The day of advertisement, regardless of whether or not the applicant's claim is well-founded, may well be the day the bell tolls for the debtor. Long ago Sir Richard Malins VC,[44] recently Jacobs J, in *Re Golden Breed Pty Ltd,*[45] and

37 [1968] 2 All ER 769, 773.
38 See later discussion of locus standi in context of cross-claims as grounds of substantial dispute.
39 [1977] ACLC 29,422.
40 Ibid 29,427.
41 [1976] ACLC 28,634, 28,643.
42 [1967] Qd R 218, 225.
43 [1978] ACLC 30,121, 30,129.
44 In *Cadiz Waterworks Co* v *Barnett* (1874) LR 19 Eq 182, 195-197: "the advertising of such an application would...inflict irreparable injury on the Plaintiffs..." (196).
45 (1979) 22 SASR 392, 392-393; [1979] 85 LSJS (SA) 109-110.

Barker J in *Universal Chemicals Ltd* v *Hayter*[46] among others,[47] commented on the potential embarrassment and financial handicaps a company could suffer if subject to mere presentation and advertisement of a winding up petition. Creditors, clients and customers will naturally be very cautious in future dealings with the company, especially as under s 365(2) [s 223(2) UCA] winding up is deemed to have commenced at the time of presentation of the application. Dispositions thereafter are void unless they are protected by a s 368 [s 227 UCA] order. The company's commercial reputation suffers: credit dries up, banks may refuse to honour cheques drawn on the company's accounts, the realizable value of the company's assets may slump, and leases and mortgages may be terminated or called up. Many debentures, for example, provide that mere presentation of a winding up application or petition is evidence of default. Struggling companies thus may be prematurely doomed. Also, presentation against one company in a group may seriously affect the group as a whole. The court is willing to consider the consequences of presentation on associated persons and companies,[48] and is sensitive to the dangers to companies, their shareholders and employees, from the mere publication of a presentation. Of course not all companies will suffer from such advertisement — some have no commercial creditworthiness to lose; others would not usually be affected by public knowledge of a petition, (for example, companies that do not trade or that have suspended active business).

The court exercises a wide discretion in winding up hearings to dismiss or adjourn the hearings, or make such other orders as it thinks fit. And the court seems to prefer dismissal of the application to mere adjournment or standing over for matters in contest to be cleared up.[49] Generally it does not take the latter course unless it doubts that the company will be able to pay the debt if one is established by separate proceedings.[50] It would be most unusual if the court merely stood over an application (in preference to dismissing it) where a solvent company raised a substantial dispute. There are other more suitable avenues for settling and recovering debts than "this vexatious mode of proceeding

46 Unreported, Auckland Supreme Court (A1809/79, 7 March 1980).

> "From a commercial point of view, the issue and, more especially, the advertisement of a winding-up petition, justified or unjustified, can have a devastating effect on a company. Trade creditors, bank managers and the like become understandably perturbed when notice of the issue of a petition is advertised in the newspapers. Often, in my experience, the assurances of company management to such persons that all is well financially with the company are greeted with some scepticism, even in those cases where the ground of the petition is not inability to pay debts but the "just and equitable" ground founded upon some internal strife. It is easy to issue and advertise the petition without the company's knowledge. An injunction after that stage may not repair the damage done by the advertisement."

47 See also McGarvie J in *Fortuna Holdings Pty Ltd* v *FCT* [1976] ACLC 28,634, 28,657; *Charles Forte Investments Ltd* v *Amanda* [1964] 1 Ch 240, 252, 261; *Dow Securities Pty Ltd* v *Manufacturing Investments Ltd* [1981] ACLC 33,173, 33,176; *Re Wiltshire Iron Co* (1868) 3 Ch App 443, 446-447; *Re Mal Bower's Macquarie Electrical Centre Pty Ltd* [1974] 1 NSWLR 254, 256-257.

48 *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,657.

49 See, eg, Bowen CJ in *Re Madison Avenue Carpets Pty Ltd* [1975] ACLC 27,895, 27,897 and authorities cited there.

50 See *Re QBS Pty Ltd* [1967] Qd R 218, 226 per Gibbs J; *Re Horizon Pacific Ltd* [1977] ACLC 29,422, 29,427. See also Zelling J in *Re Vivre Boutique Pty Ltd* [1981] ACLC 33,227, esp 33,230-33,231.

[the winding up proceedings]..." [51] It is quite possible too that the court may, as it did in *Cadiz Waterworks Co* v *Barnett,*[52] and recently in *Vanguard Insurance Co Ltd* v *Darley Trading Pty Ltd,*[53] question the motives of an applicant where a solvent company is involved.

In exercise of its inherent jurisdiction to prevent abuse of its process the court will, where appropriate, restrain by injunction the presentation of an application so that the advertisement will not go ahead; intervention after presentation may be too late for the company. It is better to incur the cost and delay of properly determining the issue than risk damage by premature advertisement. McGarvie J in *Fortuna Holdings Pty Ltd* v *FC of T* [54]stressed that the possibility of irreparable damage to the company was the basis for injunctive interference. That is the common element in two distinct situations or branches either of which, in his Honour's opinion, should exist before such relief can be granted: first, where the presentation might cause irreparable harm and the proposed application has no chance of success; second, where the applicant asserts a disputed claim by a procedure which might cause the company irreparable damage rather than by a more suitable alternative remedy.

Understandably the court's exercise of this discretion will be affected by whether or not a company is solvent. Advertising may be a public service where an insolvent company is involved: contrariwise solvent companies are likely to suffer much and probably unjustifiably from the advertisement.[55] Even after presentation an injunction may still be issued restraining its advertisement, if there is a likelihood of serious damage to the company.[56] However the court lacks jurisdiction to restrain the *service* of a demand, as, "no matter how disputed the debt may be, [a service of a demand] is not an unlawful act, nor in my opinion can it be said to infringe any right of the alleged debtor." [57]

The court is also mindful of possible injustices to petitioners. Multiplicity of proceedings and excessive delays can seriously affect a

51 Sir R Mallins VC in *Cadiz Waterworks Co* v *Barnett* (1874) LR 19 Eq 182, 194.
52 Ibid 194-196.
53 (1981) 1 ANZ Insurance Cases 77,311, 77,315.
54 [1976] ACLC 28,634.
55 See Lucas J in *Community Development Pty Ltd* v *Engwirda Construction Co* [1968] Qd R 541, 547. He asked rhetorically: "What irreparable injury can then be done to an insolvent company by the advertisement of a petition for a winding up order?" This passage was cited by McGarvie J in *Fortuna Holdings Pty Ltd* v *Federal Commission of Taxation* [1976] ACLC 28,634, 28,655. His Honour noted: "It is primarily for the purpose of assessing the reality of the risk of damage through the mere presentation of a petition, that courts take into account the solvency of the company in considering whether to restrain presentation of a petition." In that case Fortuna Holdings Pty Ltd (one of eight companies subject to petition) was in a doubtful financial position and McGarvie J said he was not satisfied the company was solvent, even when the amount of tax due was left out of account. The court refused to restrain the presentation of the petition against Fortuna. (See comment on this case later). In *Re Clem Jones Pty Ltd* [1970] QWN 14 the solvency of the company combined with a bona fide counterclaim against the petitioner led to Matthews J restraining, by injunction, further proceedings upon the petition.
56 *Re A Company* [1894] 2 Ch 349; *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,637.
57 *Altarama Ltd* v *Camp,* unreported, NSW Supreme Court (No 1854 of 1980, 4 July 1980) per McLelland J. See also *Re a Company* (1980) 35 ACTR 36, where a petitioner gained leave to withdraw a petition from the Court list, before it was published, to prevent serious impairment to the company's credit.

would-be applicant. The spectre of eroding assets troubles creditors and is often put to the court.[58] As Buckley LJ reminded his court in *Bryanston Finance Ltd* v *de Vries (No 2):*

> "It has long been recognised that the jurisdiction of the court to stay an action in limine as an abuse of process is a jurisdiction to be exercised with great circumspection and exactly the same considerations must apply to a quia timet injunction to restrain commencement of proceedings. These principles are, in my opinion, just as applicable to a winding up petition as to an action . . . The restraint of a petition may also gravely affect the would-be petitioner and not only him but also others, whether creditors or contributories." [59]

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58 Eg, in *Thiess Peabody Mitsui Coal Pty Ltd* v *AE Goodwin Ltd* [1966] Qd R 1, 7; *Re Restaurant Chevron Ltd* [1963] NZLR 225, 229; *Re Vivre Boutique Pty Ltd* [1981] ACLC 33,227, 33,228, 33,230, 33,231. The court may also heed pleas on behalf of future creditors. But see Ungoed-Thomas J in *Mann* v *Goldstein* [1968] 2 All ER 769, 774-775, where he dismissed a petition even though the company was insolvent and even though it could have been argued "it would be to the detriment of future possible creditors to countenance the continuation of a company unable to pay its debts as they fall due."

59 [1976] Ch 63, 78. This statement of Buckley LJ was cited approvingly by Goulding J in *Holt Southey Ltd* v *Catnic Components Ltd* [1978] 1 WLR 630, 632, and Zelling J recently in *Re Vivre Boutique Pty Ltd* [1981] ACLC 33,227, 33,230. See also McGarvie J considering a request for an interlocutory injunction to prevent presentation of a petition in *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,657:

> "[Counsel] submitted that the principles which I should apply in determining the application for the interlocutory injunction are those of *Beecham Group Limited* v *Bristol Laboratories Pty Limited* (1968) 118 CLR 618 rather than any different principles which may flow from *American Cyanamid Co* v *Ethicon Ltd* [1975] AC 396. I consider this to be the correct approach: *Firth Industries Ltd* v *Polyglas Engineering Pty Ltd* (1975) 49 ALJR 263. However, in an application for an interlocutory injunction in a case of this type, there seems, since the decision in *Bryanston Finance Ltd* v *De Vries (No 2)* (1976) 2 WLR 41, to be little if any difference between the approach in Australia and the approach in England.
>
> I have approached the question by first inquiring whether the plaintiffs have made out a prima facie case, in the sense that if the evidence remains as it is, there is a fair probability that they would succeed if this action came for trial. I have decided that the plaintiffs have not made out this prima facie case."

See also Bray CJ in *Pizzey Ltd* v *Classic Toys Pty Ltd* [1975] ACLC 28,011, 28,014:

> "There is no doubt that in order to establish a right to an interlocutory injunction a plaintiff has to show, firstly, some sort of prima facie case and, secondly, that the balance of convenience is in favour of the injunction. The degree of strength of that prima facie case has been variously put. In *Beecham Group Ltd* v *Bristol Laboratories Pty Ltd* 118 CLR 618 at p 622 it was said by the learned judges of the High Court that "if merely pecuniary interests are involved 'some' probability of success is enough". The lowest degree of probability is, in my view, a chance of a microscopic fraction over 50% that the event in question will occur. But I am prepared again in the plaintiffs' favour to assume that an arguable case for the counterclaim would be enough."

Bray CJ's mathematical explanation accords with the common meaning of "probable". But Lord Hodson in *The Heron II, Koufos* v *Czarnikow Ltd* [1967] 3 A11 ER 686, 707, while acknowledging the common meaning was that "something is more likely to happen than not," noted that the word need not have that "narrow meaning." Spry in (1981) 55 ALJ 784 argues against limiting the flexibility of the court in granting equitable remedies. He suggests the degree of likelihood of success that should be shown is, in the words of Mahoney JA in *Shercliff* v *Engadine Acceptance Corp Ltd* [1978] 1 NSWLR 729, 737, "that which the Court thinks sufficient, in the particular case, to warrant preservation of the status quo", and no more.

Winding up orders issued as a matter of right?

Gibbs J in *Re Leonard Spencer Pty Ltd* echoed high authority in noting:

> "A creditor whose debt is undisputed and who cannot obtain payment is entitled *ex debito justitiae* [as a matter of right] to a winding up order."[60]

Some courts even insist there is a duty cast on the court to grant a winding up order as of right wherever the legislature's requirements as to standing and procedure are met.[61] This view has the virtues of clarity and blunt justice: pay up or be wound up. Lord Cranworth appears to be quite dogmatic in *Bowes* v *Hope Life Insurance and Guarantee Co:*

> "It is not a discretionary matter with the Court when a debt is established and not satisfied to say whether the company shall be wound up or not; that is to say, if there be a valid debt established, valid both at law and in equity."

But he then adds:

> "One does not like to say positively that *no* case could occur in which it would be right to refuse it, but, ordinarily speaking, it is the duty of the court to direct the winding up." [62]

The word "may" and not "shall" is used in s 364(1). A discretion exists, although sparingly used when the statutory criteria are otherwise met.[63] The court has refused winding up orders or granted injunctions where, for example, the petitioner exhibited an improper motive, where a majority by value of creditors opposed the order, where the petitioning creditor had some other remedy than the drastic step of winding up,[64] or where the petitioner stood to benefit little from a winding up order.[65]

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60 [1963] Qd R 230, 233. See also Irvine CJ in *Re Concrete Pipes and Cement Products Ltd* [1926] VLR 34, 38-39.

61 See *Re Chapel House Colliery Co* (1883) 24 Ch D 259, 270. See also Bowen CJ in *Re Roma Industries* (1976) 1 ACLR 296, 298: "As a general rule a creditor who cannot obtain payment is, as between himself and the company that owes the debt, entitled to a winding up order as a matter of right (*IOC Australia Pty Ltd* v *Mobil Oil Australia Ltd* (1975) 49 ALJR 176 at p 182)."

62 [1865] 11 HLC 389, 402. This case was cited in *Re Concrete Pipes and Cement Products Ltd* [1926] VLR 34, 38 by Irvine CJ. His Honour, however, applied the statutory discretion in that case to dismiss a petition presented by a creditor even though the creditor had fulfilled the prima facie statutory requirements. Edmund-Davies LJ in *Re LHF Wools Ltd* [1970] Ch 27, 41 cited Lord Cranworth in full (ie with the qualifying words) to contradict any suggestion that a companies court is "powerless" once a debt is established and not satisfied. See also Gibbs J in *IOC Australia Pty Ltd* v *Mobil Oil Australia Ltd.* (1975) 49 ALJR 176, 182.

63 See Virtue SPJ in *Re First Western Corp Ltd* [1970] WAR 136, 138, citing Myers CJ in *Tench* v *Tench Bros* [1930] NZLR 403, 406. See also O'Bryan J in *Re KL Tractors Ltd* [1954] VLR 505, 512.

64 See McGarvie J in *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,643. The creditor need not, it seems, exhaust all other legal means of enforcing payment before resorting to a winding up: *Re Roma Industries Pty Ltd* (1976) 1 ACLR 296, 298.

65 See *Re St Thomas's Dock Co* (1876) 2 Ch D 116, 121: "the Petitioner does not allege or pretend he can get any money out of the winding-up order..."

Often the opponents of a winding up hope that given time and proper management the debtor company will trade itself out of trouble.[66]

The companies code already provides, in s 315 NCA [s 181 UCA], a procedure whereby, through a scheme of arrangement, a sufficient majority of creditors may allow a company a chance to trade out of difficulties. In addition s 431(1) NCA [s 289(1) UCA] provides:

> "The Court may, as to all matters relating to the winding up of a company, have regard to the wishes of the creditors or contributories as proved to it by any sufficient evidence..."

The words "all matters relating to the winding up of a company" certainly embrace the question of whether or not a winding up order should be pursued or issued.[67] The use of "may" indicates that while the court, exercising its discretion judicially, must have regard to, it need not give effect to, the wishes of other creditors or of contributors.[68] And, as Willmer LJ pointed out in *Re P & J Macrae Ltd;*

> "the important words 'as proved to it by any sufficient evidence' [in the statute]...to my mind can only be construed as imposing a duty upon creditors to give adequate reasons in justification of the wishes they express." [69]

Simple opposition, without more, would clearly be insufficient.

Interpreting the predecessor of s 431(1), Irvine CJ in *Re Concrete Pipes and Cement Products Ltd* [70] ruled that a winding up petition is not for the benefit of the petitioner alone but also for the benefit of the class to which he belongs. Once a court is seized of such an application it should consider the interests of the other creditors, particularly those of a majority (numerically or, especially, by value) if that majority opposes an order. Pape J in *Re Metropolitan Fuel Pty Ltd* cautioned:

> "it is for the court to examine the reasons given by the majority of the creditors for itself, and ... it should not give effect to them simply because they are the wishes of the majority, but ... in deciding whether such wishes should prevail, it should consider whether it is just and equitable to give effect to them. The burden of showing that it is not just and equitable that the wishes of the majority should prevail would appear from the *Melbourne Carnivals Case* to be on the petitioning creditor."[71]

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66 In *Re Melbourne Carnivals Pty Ltd (No 1)* [1926] VLR 283 the court acknowledged that those opposing a petition on the grounds that the company could trade out of its difficulties would probably be unable to displace the prima facie right of the petitioner to have the company wound up. But this depends on the facts of the case. In *Re St Thomas's Dock Co* (1876) 2 Ch D 116 Jessel MR stood over a petition for six months to allow the company the chance to become profitable.

67 See Pape J in *Re Metropolitan Fuel Pty Ltd* [1969] VR 328, 331; Weighall A-J in *Re Melbourne Carnivals Ltd (No 1)* [1926] VLR 283, 290; *Re Roma Industries* (1976) 1 ACLR 296, 298-299; *Re St Thomas's Dock Co* (1876) 2 Ch D 116, 121.

68 See Upjohn LJ in *Re P & J Macrae Ltd* [1961] 1 WLR 229, 237.

69 [1961] 1 WLR 229, 235. Woodhouse J cited this passage with approval in *Re Restaurant Chevron Ltd* [1963] NZLR 225, 228. Cf *Buckley on the Companies Acts* (13th edn 1957) 450.

70 [1926] VLR 34, 38-39.

71 [1969] VR 328, 332.

The weight of authority suggests that rarely will the interests of the other creditors override those of the applying creditor. Certainly, as Buckley LJ reaffirmed in *Re Southard & Co Ltd,*[72] the mere fact that a majority by value of creditors opposes the petition is not decisive.[73] Size, of course, goes to persuasiveness.[74] But a creditor who has established his standing has a prima facie right to a winding up order. Only exceptional circumstances lead the court to deny that right. In *Re Roma Industries,*[75] for example, the Commissioner of Taxation's petition was unsuccessfully opposed by the only other major creditor, even though she was owed $130,792 by the company, well over three times the alleged tax debt of about $36,000.[76]

The class to which the opposing creditor(s) belongs may be influential,[77] but only "outside" creditors, and proportionately very substantial ones in total value at that, seem to have any clout under s 431. This does not seem unreasonable. Otherwise the section would undermine the desirable simplicity and convenience of the demand procedure, and there would be little point in the legislation setting out relatively low minimum indebtedness requirements in s 364(2)(a). Creditors who oppose winding up should act before the application is heard.

Creditor must have a bona fide purpose

It is well settled that the creditor seeking a winding up for insolvency must have what is termed a "bona fide purpose". This does not mean that the creditor must feel no hostility towards the company. As Gibbs J pointed out in *IOC Australia Pty Ltd* v *Mobil Oil Australia Ltd,* "it is not the law that only a creditor who feels goodwill towards his debtor is entitled to a winding-up order."[78] However the applicant must act

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72 [1979] 1 WLR 1198, 1205.

73 See *Re Southard & Co Ltd,* ibid; *Re Metropolitan Fuel Pty Ltd* [1969] VR 328, 332; *Re Vuma Ltd* [1960] 1 WLR 1,283, 1,286. Under s 431(2) [s 289(2) UCA] the court must have regard "to the value of each creditor's debt".

74 See, eg, *Re St Thomas's Dock Co* (1876) 2 Ch D 116, 120-121. See also *Re P & J Macrae Ltd* [1961] 1 WLR 229, 238 per Upjohn LJ (dissenting); *Re Restaurant Chevron Ltd* [1963] NZLR 225 per Woodhouse J. In the last case the court looked to see whether or not the opposing majority had good reason for its attitude and, finding it had none, ordered a winding up. In *Re Jacobs River Sawmilling Co Ltd* [1961] NZLR 602 creditors for and against the order were fairly evenly balanced in number and value. The court gave effect to the petitioners' prima facie right.

75 (1976) 1 ACLR 296. See also *Re Vuma Ltd* [1960] 1 WLR 1283 where the petitioning judgment creditor gained his order even though opposed by two creditors who were owed "considerably more than the amount owing to the petitioning creditor". (1284) It was material here that the opposing creditors, like those in *Re P & J Macrae Ltd*, did not file evidence explaining their opposition.

76 Her position was weakened by the fact that she was also a director, shareholder and first mortgagee of the company. This made it "difficult to distinguish her position from that of the company itself". Ibid 298-299 per Bowen CJ.

77 See McPherson, *The Law of Company Liquidation* (2nd edn 1980) 63-68. He points out that unsecured creditors, being the most vulnerable, are entitled to greater consideration.

78 (1975) 49 ALJR 176, 182. Here the company alleged that Mobil's dominant motive in prosecuting the petition was to force IOC out of business. Gibbs J noted that it was "immaterial" even if Mobil were "pleased at the prospect that the appellant might have to cease business." (182). In *Re Metropolitan Fuel Pty Ltd* [1969] VR 328 the company fruitlessly alleged the petition had been brought for the "ulterior purpose" of getting rid of competition and to satisfy a "vendetta" against the company.

without fraud, deceit or some improper and dominant ulterior motive: otherwise the court may exercise its inherent jurisdiction to prevent an abuse of its process.

In *Cadiz Waterworks Co Ltd* v *Barnett,* Sir Richard Malins VC said a winding up petition would be dismissed with costs if the court "sees a petition...presented, not for a *bona fide* purpose of winding up the company, but for some collateral and sinister object."[79] His own example of a "collateral and sinister object" was that of trying to enforce payment of a debt for a large amount when it is well known a much smaller amount is due. "Blackmailing" a company into premature payment,[80] pressuring a company to purchase the petitioner's shares[81] and stifling competition could be others. The object of the court, Sir Richard Malins added, is "to restrain the assertion of doubtful rights in a manner productive of irreparable damage".[82] Later in the same year — 1874 — Jessel MR passed a similar comment:

> "this Petition has not been presented *bona fide* — that is, not with the view of obtaining a winding up order, but with the object of extorting from the company a larger sum than they thought was fairly due, under pressure of a threat to present the winding-up petition." [83]

Proof of improper motives is, of course, difficult. Recognising such difficulties the court is reluctant to speculate about applicants' motives. On at least one occasion[84] the court ruled that before it could interfere there must be "manifestly an abuse of the process of the Court", and that the improper motive be the "sole" motive of the applicant in presenting the petition. These high standards will only rarely be met.

The bona fide purpose requirement is met, the cases say, as long as the purpose of the application is to wind up the company. Ungoed-Thomas J read Sir Richard Malin's words carefully to conclude:

> "the purpose of winding up the company is treated as a bona fide purpose in contrast to some purpose other than winding up of the company." [85]

Presumably, and Ungoed-Thomas J acknowledges as much,[86] a creditor can harbour, even express, personal hostility and vindictiveness towards the debtor company yet still be adjudged bona fide.

This interpretation of the term "bona fide purpose" is perhaps misleading. Surely a creditor's dominant *purpose* will never be to wind

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79 (1874) LR 19 Eq 182, 196.
80 See *Vanguard Insurance Co Ltd* v *Darley Trading Pty Ltd* (1981) 1 ANZ Insurance Cases 77,311, 77,315.
81 See, for example, *Tench* v *Tench Bros Ltd* [1930] NZLR 403 where the trial judge granted a stay because the petition was presented for the purpose of bringing pressure to bear on the company's directors to buy the petitioner's shares. The Court of Appeal reversed the decision but affirmed the principles expressed with respect to jurisdiction to dismiss or stay petitions.
82 (1874) LR 19 Eq 182, 196.
83 In *Re London and Paris Banking Corporation* (1874) LR 19 Eq 444, 448.
84 In *Re First Western Corp Ltd* [1970] WAR 136, 138 per Virtue SPJ.
85 [1968] 2 All ER 769, 772-773.
86 Ibid 772. See also Gibbs J in *IOC Australia Pty Ltd* v *Mobil Oil Australia Ltd* (1975) 49 ALJR 176, 181-182.

up a company (although that may be his intention). His purpose will invariably be to get paid, and no doubt he will be only too happy if the company can pay out and still remain in existence. Winding up is not his purpose but rather his means.[87]

It would certainly be clearer if the court put aside the use of the phrase "bona fide purpose" and its given meaning, ie the purpose of winding up the company. It may be enough if the court simply asks; is the applicant's dominant purpose that of getting paid? Could one go further and say that a creditor's purpose or motives are irrelevant as long as the statutory requirements are met? Let the debtor get his house in order or face the consequences, one may argue: let the court's discretion remain only for rare and exceptional cases.

No doubt some creditors will take more satisfaction than others in winding up the debtor. A vindictive creditor attracts little judicial sympathy. But the bandying about of words and phrases such as "bona fide", "extortion", "collateral and sinister objects", "blackmail" and "scandalous abuse of the process of the court" generates more emotion than assistance when the court is exercising its discretion. The vital issues are whether or not the applicant has locus standi and has faithfully followed the statutory procedures. The motives of the creditor in seeking a winding up should but rarely influence the court's exercise of its discretion, and then perhaps only when the company is solvent. But even then the court should be satisfied the company has a substantial dispute or cross-claim before turning away an application. The existence and airing in court of improper motives does not assist in that enquiry either.

A disputing debtor must show substantial grounds of dispute

The phrase "bona fide" also appears in the established test for the adequacy of a debtor's dispute of the debt. Just as a creditor's purpose in seeking a winding up must be bona fide, so too must any successful dispute of indebtedness by the company. Once again the words "bona fide" do not accurately describe the test. It can be more clearly stated — "is the debt disputed on substantial grounds?" Lord Greene in *Re Welsh Brick Industries Ltd* confirmed this when he spoke of "considering whether or not the dispute is a bona fide dispute, or, putting it another way, whether or not there is some substantial ground for defending the action." [88]

The creditor must ensure the debt is prima facie proved. It is not prima facie proved if the debtor company raises what is objectively a substantial or arguable dispute, one that cannot be tried on an interlocutory application but which must be tried in separate proceedings.[89] Usually when a substantial dispute arises over indebtedness

87 As McGarvie J put it in *Fortuna Holdings Pty Ltd* v *Deputy Federal Commissioner of Taxation* [1976] ACLC 28,634, 28,643: "Usually in a creditor's petition, the only interest and legitimate object of the creditor is to get paid..." Jessel MR in *Re St Thomas's Dock Co* agreed: (1876) 2 Ch D 116, 118.

88 [1946] 2 All ER 197, 198. Gibbs J cited this passage with approval in *Re QBS Pty Ltd* [1967] Qd R 218, 225.

89 See Malins VC in *Re Imperial Silver Quarries Co Ltd* (1868) 16 WR 1220, 1221: "It is against the principles of this Court to wind up a company either (1) upon a disputed debt, or (2) if it is clear that on the debt being established it will be paid. But as to

other proceedings are required before the application can progress.[90] As noted above, until such disputes are resolved the applicant's standing under s 363 is in doubt.

A simple denial of the debt by the company is insufficient.[91] The grounds for denial must be substantial.[92] Such grounds were found in a lengthy list of disputes — including allegations of breach of promise, of breach of contractual clauses, of cross-claim and part payment — in *GB White* v *Taylor Railtrack Pty Ltd.* The issues between the parties, Needham J said, could not be described or "dismissed as frivolous or not substantial".[93] His Honour explained his role:

> "It is not for me on this application, having reached that conclusion [that there are substantial issues in dispute], to determine the issues between the parties, nor, I think, to separate out the issues which I think are substantial from any which may not be so considered. The procedure given by s 222 of the *Companies Act* is one given to a "creditor". Where an alleged creditor seeks to take advantage of those procedures before establishing his debt in the ordinary course, and seeks to use them against a solvent company, I think the Court should be most wary of shutting the company out from its right to have its liability determined in accordance with the process given by law for that purpose."[94]

Many pleas for restraint of winding up proceedings are rejected. In *Re Damons Insurance Brokers Pty Ltd* [95] for example, an insurance broking firm unsuccessfully sought the continuation of an injunction restraining the petitioners from advertising the petition. The brokers alleged that the petitioner — an insurer -- had gratuitously exonerated the brokers from payment of overdue premium payments. But the company, Needham J concluded, had failed to show its "alleged defence is not frivolous".[96] So too in *Bateman Television Ltd* v *Coleridge Finance Co Ltd.* [97] The

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89 *Cont.*
the first point, the dispute must be one in which the Court feels that there is substance, so that it cannot be decided on interlocutory application." See also *Re Horizon Pacific Ltd* [1977] ACLC 29,422 where the dispute centred on defective execution of a deed under seal. Needham J held this was not a case where the questions in dispute could be decided on the contents of the petition and the affidavits in reply.

90 See Gibbs J in *Re QBS Pty Ltd* [1967] Qd R 218, 225.

91 See North P in *Bateman TV Ltd* v *Coleridge Finance Co Ltd* [1969] NZLR 794, 808 (CA), on appeal [1971] NZLR 929 (PC); Gibbs J in *Re QBS Pty Ltd* [1967] Qd R 218, 225. See also Jessel MR in *Re Great Britain Mutual Life Assurance Society* (1880) 16 Ch 246, 253: "...in my opinion it is not sufficient for the Respondents upon a petition of this kind, to say, 'We dispute the claim'. They must bring forward a *prima facie* case which satisfies the Court that there is something which ought to be tried, either before the Court itself, or in an action, or by some other proceeding." This passage was cited by North P in *Bateman TV* (809).

92 In fact little enough is required of the company to show a substantial or bona fide dispute. Discussed below.

93 [1978] ACLC 30,100, 30,105.

94 Ibid.

95 [1979] ACLC 32,027.

96 Ibid 32,030. *Stonegate Securities Ltd* v *Gregory* [1980] Ch 576 provides a novel category of substantial dispute where the petitioner relies on a statutory demand. There the company disputed in good faith that the debt was *presently due*, although it conceded being a contingent creditor. Thus para (a) was not available to the creditor, and he had not satisfied the requirements of para (c).

97 [1969] NZLR 794 (CA); [1971] NZLR 929 (PC).

existence of the required debt was sufficiently proved by oral and documentary evidence in the lower court hearing. A substantial dispute was not raised.[98]

One might reasonably expect that the solvency of a company may be influential in the court's decision as to whether there was a substantial dispute warranting rejection of a petition. There are ample dicta in this vein.[99] Yet in *Mann* v *Goldstein,*[100] perhaps the first decision directly on the point, both companies subject to a threat of winding up were insolvent. Still the prosecution of the petitions was restrained: the petitioners had not established their standing. An admittedly insolvent company also convinced the court to dismiss a winding up petition in *Re Glenbawn Park Pty Ltd.*[101] It can be argued that would-be creditors have a right to be warned of the company's insolvency, and that the application ought to be advertised and proceedings continue even where the applicant's claim and thus his standing is disputed on substantial grounds. On the other hand one can point out that such proceedings seriously prejudice a company's chances of recovery, and that only a true creditor should exercise the winding up power. The court in *Mann's* case took the latter view.[102] It is, as the court pointed out, relatively easy in such circumstances to have another applicant substituted in place of the one whose debt is disputed and for proceedings then to continue.[103]

Dispute over quantum as distinct from liability

But what about the situation where the s 364(2)(a) [s 222(2)(a) UCA] notice, and where appropriate the application as well, demand more (or less, for that matter) than is due but it is established that at least $1,000 (or whatever the current minimum indebtness requirement may be) is owed by the company? [104] This question was briefly adverted to by Needham J recently in *Re The Daily Pty Ltd.*[105] While acknowledging its

98 Cf *Thiess Peabody Mitsui Coal Pty Ltd* v *AE Goodwin Ltd* [1966] Qd R 1, 8-9 where Stanley J found enough evidence in the affidavit of the company's secretary and solicitor to evidence a "genuine dispute" (and to satisfy the court that the company was solvent).

99 See *Bateman's* case [1969] NZLR 794, 819-820; *Community Development Pty Ltd* v *Engwirda Construction Co* [1968] Qd R 541, 546-547. See also Gibbs J in *Re QBS Pty Ltd* [1967] Qd R 218, 224-225: "It has been held that this rule [that a bona fide dispute by the company is grounds for refusal or suspension] does not apply if the company is insolvent (*Re A Private Company* [1935] NZLR 120)..."

100 [1968] 2 All ER 769.

101 (1977) 2 ACLR 288.

102 Cf Lucas J in interlocutory proceedings in *Community Development Pty Ltd* v *Engwirda Construction Co* [1968] Qd R 541, 547. He thought consideration of the locus standi of the petitioner should be carried out "upon the hearing of the petition".

103 See [1968] 2 All ER 769, 775. In *IOC Australia Pty Ltd* v *Mobil Oil Australia Ltd* (1975) 49 ALJR 176 the first petitioner (another company) was granted leave to withdraw its petition and an order was made substituting Mobil Oil as petitioner. Rule 28 of the Rules of Court (Companies Act) 1965 (SA) deals with substitution of petitioners. If the first petitioner fails to appear, or apply for an order, or consents to withdraw his petition, or allows it to be dismissed or adjourned, the court may substitute any other creditor as petitioner. Thus, although several different petitions may be presented against a company, they will rarely be necessary.

104 This question is discussed by Barton, "The Law Relating to Disputed Indebtedness Where the Winding-Up of a Company is Sought on the Ground of Inability to Pay Debts" (1981) 9 Aust Bus LR 94, 100-105.

105 Unreported, NSW Supreme Court judgment (No 2437, 19 December 1980).

importance, he chose not to give an opinion one way or the other on the submission that a notice that claimed more than was due was invalid.

> "Mr Rayment, for the company, submitted that, although it was a generally accepted view in the profession that a section 222 notice claiming more than the amount found to be due was valid provided it was held that at least $100 was owed, the decisions supporting that view failed to distinguish between the validity of such a *notice* and the availability of a winding up order where the petitioner, in his *petition,* claimed to be owed a sum in excess of that proved provided the latter sum fulfilled the minimum requirement. [Emphasis added]. He submitted that there was no question of the validity of a notice in *Re Tweed Garages Ltd* [1962] Ch 406 or *Re Metropolitan Fuel Pty Ltd* [1969] VR 328, and that the reliance upon those cases by Kaye J in *Re Convere Pty Ltd* [1976] VR 345 to uphold a notice which claimed more than was due was incorrect and that the latter case was wrongly decided. He also submitted that the decision of Yeldham J in *Re Glenbawn Park Pty Ltd* (1977) 2 ACLR 288 contained a similar error. The terms of s 222(2)(a) were said to require that the benefit of the statutory presumption should go only to those whose notices required the company "to pay the sum so due" and in cases of companies who "neglected to pay the sum". The benefit of the presumption should not be extended to those who failed to comply in every way with the conditions of its arising.
>
> As I have said, it is not necessary for me to determine this important question in this case. I merely note the submission and express the view that it has substance."

Counsel appears to have put much the same argument as that unsuccessfully argued by the company's counsel in *Cardiff Preserved Coal and Coke Co* v *Norton*[106] over a slightly differently worded provision. In *Cardiff* the company alleged that as the demand specified £628 and the creditor was in fact only entitled to £411-7-9 the winding up order was bad. Lord Chelmsford LC was rather less impressed by this argument than Needham J was with the similar argument in *Re The Daily Pty Ltd.* Although the sum demanded was more than was due, Chelmsford LC ruled "the company neglected to pay 'such sum', *which means not the sum demanded, but the sum due,* which they might have paid, and so have prevented the order being made."[107] [Emphasis added.]

The equivalent of the words "such sum" in the current Australian legislation is "the sum so due" (s 364(2)(a)). In summary the question raised in *Re The Daily Pty Ltd* appeared to be: as the wording of paragraph (a) specifies that the demand must be for "the sum so due" and the presumption arises only when the company has neglected to pay "the sum", should the demand not specify the exact sum due, and not

106 (1867) 2 Ch App 405, 410. The provision before the court was the Joint Stock Companies Act 1856, s 68. (This statute was adopted in SA in 1864). The words "such sum" were replaced by "the sum so due" in the Companies (Consolidation) Act 1908, s 130(i) (UK).

107 Ibid. This passage was cited with approval by Stanley J in *Thiess Peabody Mitsui Coal Pty Ltd* v *AE Goodwin Ltd* [1966] Qd R 1, 6.

some greater (or lesser) amount? Could the company not argue that, where a greater or lesser sum than the demanded amount is found to be owing on the hearing, the creditor has not complied exactly with the wording of the provision? Is the petitioner's demand thus invalidated?

This question arose again recently over an understated demand in *Vanguard Insurance Co Ltd* v *Darley Trading Pty Ltd.*[108] The defendant had served a notice on an insurance company demanding $6,000, being a portion only of the value of a stolen vehicle claimed by the defendant under its policy with the company. The insurance company was solvent but proposed, in accordance with its usual practice, to delay its payment under the policy for 90 days. Within approximately two weeks of the theft the defendant had served the demand. Needham J adverted to the question of the validity of the demand. It had claimed $6,000 "being part of the amount owing by you to the creditor in accordance with the provisions of the policy". The insurance company's claims manager had told the defendant the car was worth $7,500. Needham J commented:

> "...the notice which Mr Conway served on behalf of the defendant does not even claim to demand that sum. [Presumably here his Honour refers to the full value of the vehicle.] It may well be that, in order to obtain the benefit of s 222(2)(a), the creditor must do as the statute says, namely, serve a notice requiring the debtor to pay the sum so due.
>
> I do not think I need to determine this issue in this case because it is plain on the face of the notice that the notice does not purport to claim the sum due. It is not enough, in my opinion...that a creditor or a person who claims to be a creditor should issue a s 222 notice for any amount whether in excess or less than the amount which the creditor claims provided it exceeds $100." [109]

Without for a moment questioning the decision in the case (the company gained an injunction to stop presentation) this quoted statement offers a narrow view of what the phrase "the sum so due" means. Surely the phrase does not mean or suggest that the company's total indebtedness to the creditor, or even one distinct debt, must be stated in the demand. Fixing an exact quantum will often be almost impossible, yet frequently it may be patently obvious that a large sum — much more than $1,000 — is owed by the company. Why should a creditor not be able, at least for the purpose of serving a demand and getting the liquidation under way, to demand an amount that turns out to be more or less than is owing to him, as long as at least $1,000 is uncontestably due and payable? What happens in a current account situation where a company owes a creditor what amounts to a series of debts and the creditor issues a demand for only some of these debts? Is such a demand invalid?

There has been plenty of judicial comment on overstated debts, whether the overstatement is in the demand and/or the petition. There are two groups of authorities: those where overstatement was in the demand and where the demand procedure was relied on; and those where the debt was overstated but the demand procedure was not relied on by the

108 (1981) 1 ANZ Insurance Cases 77,311.
109 Ibid 77,315.

petitioning creditor. Into the latter and uncontroversial category falls *Re Metropolitan Fuel Pty Ltd* [110]. The successful petitioning creditor there claimed £243-13-3 in overdue wages from the company. Pape J found that at least £80-6-0 was owing and that this was enough to support the petition. He noted that "where there is a dispute as to part only of the debt, courts have still made winding up orders..." [111] Pape J cited *Re Tweeds Garages Ltd.*[112] There the petition was founded on the company's inability or refusal to pay an alleged debt of £20,039-19-3. There is no indication that a statutory demand was issued. The company admitted the existence of a debt but disputed the quantum. Plowman J granted a winding up order.

> "Moreover, it seems to me that it would, in many cases, be quite unjust to refuse a winding-up order to a petitioner who is admittedly owed moneys which have not been paid merely because there is a dispute as to the precise sum owing." [113]

Then there are the statutory demand cases. *Cardiff Preserved Coal and Coke Co* v *Norton* is discussed above. Recently in *Re Glenbawn Park Pty Ltd* Yeldham J claimed:

> "If such a dispute [as to indebtedness] was as to the amount only, some part of it admitted, that would not suffice [as a bona fide dispute]..."[114]

As Yeldham J points out, a dictum in *Re Convere Pty Ltd* supports this. There Kaye J comments:

> "There is a body of contemporary authority that overstatement *per se* is not sufficient either to destroy the validity of the statutory notice or to create a bona fide dispute as to the existence of the debt, provided the amount not in dispute would entitle the petitioner to a winding up order."[115]

Bowen CJ in Eq in *Re Madison Avenue Carpets Pty Ltd,* another statutory demand case, was equally unequivocal:

> "The fact that a demand turns out to be for too much will not prevent it from being effective, if more than the statutory minimum was owing..." [116]

McCarthy J in the New Zealand Court of Appeal in *Bateman Television Ltd* v *Coleridge Finances Co Ltd* [117] addressed a similar problem. Counsel for the company alleged it was not clear that $8,704.46 (the sum stipulated in the demand and petition) was owing and a winding up should not have been ordered in the lower court. McCarthy J was unimpressed. In his dictum he did not distinguish between demand and petition: he spoke generally of the debt.

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110 [1969] VR 328, 329.
111 Ibid.
112 [1962] Ch 406.
113 Ibid 413. See also *Palmer's Company Law* (22nd edn 1976) vol 1, 886.
114 (1977) 2 ACLR 288, 292.
115 [1976] VR 345, 350.
116 [1974] ACLC 27,895.
117 [1969] NZLR 794.

> "It is true that, normally speaking, the procedure of petition for a winding-up order is not a satisfactory one to dispose of the question whether a particular debt is or is not owing; but there is authority, and not a little of it, to the effect that though there may be a *bona fide* dispute concerning the precise indebtedness of the debtor, if it is patent that there is sufficient owing to found a petition and that the company is insolvent, an order will be made."[118]

His Honour does go on to caution that the proposition should not be applied too liberally: "if there is a *bona fide* substantial challenge to the debt the better course is to require establishment by action in the normal way. *A fortiori,* when the challenge is to the whole amount...."[119]

These authorities either directly or indirectly favour the view that overstatement *per se* does not invalidate a demand. *Re the Brighton Club and Norfolk Hotel Co (Ltd)* [120] does not directly contradict that. There the petitioner established that something in excess of £50 was due to him in a building contract dispute. Sir John Romilly MR in his brief 1865 judgment does not make it clear whether the state of account was so vague that it was impossible for the parties to have isolated the uncontested from the contested part of the debt. Building contracts often provide special difficulties because of their complex nature, the scope for dissatisfaction with performance, and the time taken to perform the contracts. The demand-based petition was dismissed here essentially because the judge was reluctant to wind up a "thriving business" over a contested account. He was puzzled by the apparent futility of any order he could make.

Of these cases it appears that the semantic point apparently raised by counsel in *Re The Daily* and in *Vanguard Insurance* was directly considered in only *Cardiff Preserved Coal and Coke Co* v *Norton.* As noted above, the wording of the demand provision at issue there was (immaterially in this writer's opinion) different to that in s 222(2)(a) UCA and in s 364(2)(a) NCA: ie, "such sum" instead of "the sum so due". The present wording of paragraph (a) is susceptible to both a narrow and a wide construction: ie, either "the exact sum due" or "any sum exceeding $100". The use of the definite article "the" before "sum" in paragraph (a) is simply insufficient evidence of the legislature's intention to narrow the construction; nor is such a construction called for on an ordinary reading of the provision. In paragraph (a) the phrase "the sum *so* due" refers back to the antecedent words "*a* sum exceeding $1,000 then due". Neither the exact sum due nor a single specific debt is required: merely a sum in excess of $1,000 [or $100 in UCA].

A narrow construction also affronts the common sense of the statute. Disputing the exact quantum of the debt (whether as stated in the

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118 Ibid 819-820. See also Turner J at 816.

119 Ibid 820. McPherson (*The Law of Company Liquidation* (2nd edn 1980) 47-48, 56) submits that genuine dispute as to quantum stated in a demand must lead to dismissal of the petition if the petitioner relies on non-compliance with the statutory demand, even if a portion of the debt is undisputed. *Buckley on the Companies Acts* (13th edn 1957) 459 is ambivalent.

120 (1865) 35 Beav 204; 55 ER 873.

demand or petition) may be comparatively easy. Would the smallest error in the demanded sum be fatal? If it could be then a petitioning creditor whose standing as a creditor is honest and undoubted would be denied the convenience and speed of the demand procedure by the most trivial of claims from insolvent companies anxious to stave off the fateful day.

If the court does accept the narrow construction legislative interference may be necessary to preserve this valued and workable procedure for speedily determining commercial insolvency. True, in practically all other requirements of paragraph (a) the court has demanded strict observance. Any possible ambiguity is regrettable. The legislature could introduce a provision or proviso saying that a dispute as to the precise amount (in excess of $1,000) set down in either the demand or the petition will not of itself invalidate either. Or, perhaps less satisfactorily, it could formulate more detailed provisions such as those in s 41 of the Bankruptcy Act 1966 (Cth) and those set down by the judiciary for the bankruptcy notice error, whether in overstatement or understatement. Bankruptcy notices, available to a creditor after judgment or order, are invalid if they demand less than the amount in fact due unless they indicate that any balance still owing is abandoned by the creditor. Section 41(5) provides that where the demanded sum exceeds the amount "in fact due" the notice is not invalid unless the debtor, within the time specified, gives notice (not necessarily in writing) that he disputes the validity of the notice on the basis of the mis-statement.[121] Similar rules in the winding up area might remove any ambiguity and discourage petty disputes and unnecessary litigation.

Companies that refuse to pay on demand because they dispute quantum should take care. The presumption of insolvency may still arise providing the minimum indebtedness is proved.[122] On dispute as to quantum a company, to be safe, should still pay any undisputed amount (ie, that portion of the demanded amount that it cannot challenge with substantial argument) and dispute the balance.

It is, of course, not always possible, short of a separate trial of the debt, to isolate an amount that is unquestionably due. As already mentioned, building and construction contract disputes are often difficult. *Club Marconi of Bossley Park* v *Rennat Constructions Pty Ltd* [123] and *Re The Brighton Club and Norfolk Hotel Co Ltd* are examples. In such cases a creditor should perhaps rely on s 364(2)(c) as well as (or instead of) on the demand procedure,[124] as the law clearly favours the applicant when the overstatement is simply in the application or petition. But in

121 See McDonald, Henry & Meek, *Australian Bankruptcy Law and Practice* (5th edn) para 222; Farmer, *Creditor and Debtor Law in Australia & New Zealand* (1980) 188-189.

122 Implied support for this can also be found in *Re QBS Pty Ltd* [1967] Qd R 218, 224, where Gibbs J suggested that a petition would not fail if, before the petition is presented but after the statutory three weeks demand period has lapsed, the company pays part of the amount demanded, "but remain[s] indebted to the petitioner in a sum exceeding one hundred dollars...". Ascertaining the undisputed portion of debts is not always easy, of course: see *Thiess Peabody Mitsui Coal Pty Ltd* v *AE Goodwin Ltd* [1966] Qd R 1 where a typically involved dispute between parties to a construction contract arose. See also infra n 125

123 [1980] ACLC 34,199, esp 34,202.

124 As, eg, in *Community Development Pty Ltd* v *Engwirda Construction Co* [1968] Qd R 541.

the interests of suppressing overzealous applicants yet encouraging recalcitrant debtors the more general rule seems preferable: on a demand, even an overstated or understated demand, failure to pay over or secure what the company must fairly concede, or what competent valuers consider, to be the uncontested part of the debt invites winding up.[125]

Cross-claims as grounds of substantial dispute

What is the position when the company attempts to erase its alleged and often admitted indebtedness to the applicant by alleging a cross-claim (meaning here a set-off or counter-claim)? [126] The typical case is where the applicant himself owes the debtor company an unliquidated sum usually, but not necessarily, arising from the same or a closely-related contact or transaction.[127] Such facts arose in *Re Jeff Reid Pty Ltd* recently.[128] In *Re Clem Jones Ltd* [129] evidence sufficiently disclosed that the company had in its favour a judgment for fees (for services rendered by the company in another transaction) against a partnership of which the petitioner was a member. As the company could issue execution for the whole amount of the judgment against the petitioner, and as the judgment (subject to appeal at the time of the petition hearing) was for an amount exceeding that of the petitioner's demand, Matthews J, on this and one other ground (a counterclaim), held that there was no neglect to pay the demanded sum within s 222(2)(a) UCA.

These and other cases — for example, *Re Madison Avenue Carpets Pty Ltd* [130] and *Re Convere Pty Ltd* [131] — indicate that the court treats cross-claims, if they have substance, in the same way as, because they are analogous to, disputed debts. In essence it recognises that inability to pay debts within s 364 NCA is not established where, because of a sufficient cross-claim, the overall state of account between the parties is uncertain and disputed. O'Bryan J in *Re KL Tractors*[132] had reservations

125 See *Mutual Home Loan Fund of Australia Ltd* v *Smith* [1978] ACLC 29,991, 29,992 per Needham J: "I indicated to the company that unless the amount which the company considered it owed the petitioner was paid to the petitioner, the authorities precluded me from granting any injunction to stop the advertising of the petition on the ground of a bona fide dispute as to the debt said to be owing to the petitioner by the company." See also Jessel MR in *Re London and Paris Banking Corp* (1874) LR 19 Eq 444, 446; Needham J in *Re Carmel Insurance Services Pty Ltd*, unreported, NSW Supreme Court (No 1053, 22 May 1980): "I think it is clear that, if in such circumstances the company concedes a debt, even though not the full amount claimed by the petitioner, and has failed to make any attempt to liquidate the admitted debt, the petitioner is entitled to a winding up order."

126 Cross-claim is not used in a technical sense. Lockhart J in *Re Brink; Ex parte the Commercial Banking Co of Sydney Ltd* (1980) 44 FLR 135, 138-139, in the context of ss 40(10)(g) and 41(7) of the Bankruptcy Act 1966 (Cth), discusses and contrasts the meanings of counter-claim, set-off and cross-demand. See discussion of cross-claim allegations by Barton, supra n 104 at 105-111.

127 *Altarama Ltd* v *Camp*, unreported, NSW Supreme Court (No 1854, 4 July 1980) provides a recent example of a cross-claim which flowed out of the same transaction; (a claim for damages for breach of warranty in the contract of sale that gave rise to the debt of the company).

128 [1980] ACLC 34,330.

129 [1970] QWN 14.

130 [1975] ACLC 27,895.

131 [1976] VR 345.

132 [1954] VLR 505. See also Bray CJ in *Pizzey Ltd* v *Classic Toys Pty Ltd* [1975] ACLC 28,011, 28,013-28,014.

on whether this extended to a counter-claim for unliquidated damages, but Yeldham J in *Re Glenbawn Park Pty Ltd* had no doubts:

> "if a counter-claim, whether for liquidated or unliquidated damages, and whether or not arising out of the same transaction, is based upon substantial grounds, it may be relied upon to support an argument that the company's alleged debt is disputed. Clearly the ultimate creditor is that party which recovers the largest sum upon his claim and he is a creditor only for the difference between the two verdicts of judgments." [133]

Provisions in State Supreme Court Acts (for example, s 78 of the Supreme Court Act 1970 (NSW), s 61 of the Supreme Court Act 1958 (Vic) and s 23 of the Supreme Court Act 1935-1975 (SA) [134]) have eroded the importance of distinctions between set-off and counter-claim. In any event the subtleties of difference between the two are irrelevant in the assessment of whether or not a substantial dispute as to indebtedness exists in winding up proceedings.[135]

The various Supreme Court Acts permit defendants to cross-claim against plaintiffs or petitioners whether for liquidated or unliquidated sums, and even where the sum claimed is not connected in any way with that claimed by the plaintiff or petitioner. As Yeldham J points out [136] the courts are anxious to ensure the claims of both parties are resolved if possible at the one time and for the party entitled to receive any balance upon judgment to do so. Although the determination of a cross-claim may take time, when all debts are settled the applicant may be entitled to receive nothing from the company or may even be its debtor.

The existence of a cross-claim (but only one not amounting to a legal or equitable set-off [137]) does not, in McLelland J's opinion,[138] affect the petitioner's status as a "creditor" within s 221(1)(b) UCA, even though it

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133 (1977) 2 ACLR 288, 291. Yeldham J relied on *Re Clem Jones Pty Ltd* [1970] QWN 14. Matthews J there found "The fact that the claim is in effect a counterclaim against the petitioner appears to justify a conclusion that the petitioner's debt is disputed, provided it be established that the claim is bona fide and one of substance..." (16).

134 Such provisions, as Hutley JA in *Stehar Knitting Mills Pty Ltd* v *Southern Textile Convertors Ltd* [1980] 2 NSWLR 514, 521 noted of s 78 of the Supreme Court Act 1970, allow "the adjudication of multiple conflicting claim between two parties according to their terms." Section 78 was cited in *Re Glenbawn Park Pty Ltd* (1977) 2 ACLR 288, 291.

135 *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,644, 28,649. See also *Dow Securities Pty Ltd* v *Manufacturing Investments Ltd* [1981] ACLC 33,173, 33,176.

136 In *Re Glenbawn Park Pty Ltd* (1977) 2 ACLR 288, 291.

137 McLelland J's caution here does not seem to be justified. The plea of a set-off will not affect the petitioner's status as creditor, at least until judgment on the set-off. Quite aside from the question of whether the Statutes of Set-off (2 Geo II, c 22; & Geo II, c 24) still apply in the various Australian states — they no longer apply in NSW it seems (see *Stehar Knitting Mills Pty Ltd* v *Southern Textile Converters Pty Ltd* [1980] 2 NSWLR 514) — set-off is not the equivalent of payment. Until judgment there are two separate and distinct debts. While set-off exempts the "debtor" from paying, a plea of set-off does admit the claim's existence, and until judgment on the set-off goes in the debtor's favour the creditor's claim is not extinguished. See 34 *Halsbury's Laws of England* (3rd edn) para 672, pp 395-396. See also *Re Hiram Maxim Lamp Co* [1903] Ch 70, 74-75 per Byrne J; *Re KL Tractors Ltd* [1954] VLR 505, 507 per O'Bryan J.

138 In *Re Jeff Reid Pty Ltd* [1980] ACLC 34,330, 34,333.

may be used by the court as grounds for dismissing or standing over a petition, or, perhaps, preventing the presumption of insolvency arising under s 222(2)(a). Wootten J in *Dow Securities Pty Ltd* v *Manufacturing Investments Ltd* [139] agrees. Theirs seems, with respect, a sounder finding than that of Yeldham J in *Re Glenbawn Park Pty Ltd.* Yeldham J tentatively concluded that the existence of an unliquidated cross-claim for damages based on substantial grounds meant the petitioner was not a creditor within s 222(1) UCA and thus had no standing to present the petition.[140] However claims and cross-claims are, for practical purposes, not one proceeding but two.[141] The cross-claim (used here as embracing both set-offs and counter-claims) cannot be regarded as being part and parcel of the claim. Thus until the cross-claim is adjudicated upon the claim cannot be extinguished. Further, in these cross-claim cases there is usually no dispute as to the specific debt that is the basis of the petition or application, but because of the cross-claim the company's overall indebtedness vis-a-vis the applicant may be at issue. Then the applicant will still be a creditor yet eventually may not be entitled to or be granted a winding up order.

To be a successful defence in winding up proceedings, a cross-claim must be for an amount at least equal to the debt. The limitation is well established.[142] A minor qualification may be suggested. Where the applicant relies on a s 364(2)(a) demand, the cross-claim to be effective need only be greater than the debt less $1,000 [$100 in s 222(2)(a) UCA].[143]

Simply asserting a counter claim is insufficient of course. O'Bryan J in *Re KL Tractors* [144] issued a winding up order where the company merely alleged it had claims against the Commonwealth government for a sum at least equal to the £100,000 it admitted it owed the government. Obviously any other attitude by the court would encourage what has been dubbed the "unattractive prospect" [145] of a flood of alleged cross-claims from companies seeking to avoid winding up applications.

In summary, then, the court is not concerned with distinguishing between set-offs and counter-claims. Some form of cross-claim will

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139 [1981] ACLC 33,173, 33,176.

140. (1977) 2 ACLR 288, 294.

141 See supra n 137; *Stehar Knitting Mills Pty Ltd* v *Southern Textile Convertors Pty Ltd* [1980] 2 NSWLR 514, 518 per Hutley JA: see also *Aurel Forras Pty Ltd* v *Graham Karp Developments Pty Ltd* [1975] VR 202, 218-219 per Menhennitt J; *Stooke* v *Taylor* (1880) 5 QBD 569, 575-578 per Cockburn CJ.

142 See *Re Glenbawn Park Pty Ltd* (1977) 2 ACLR 288; *Fortuna Holdings Pty Ltd* v *Federal Commissioner of Taxation* [1976] ACLC 28,634, 28,644; *Clem Jones Pty Ltd* v *International Resources Planning and Development Pty Ltd* [1970] Qd R 37; Bowen CJ in Eq in *Tranquility Holdings Pty Ltd* v *Glass Pools Pty Ltd* [1974] ACLC 27,962, 27,963. Barker J in *Universal Chemicals Ltd* v *Hayter*, unreported, Auckland Supreme Court (A1809/79, 7 March 1980) also stressed that the cross-claim must exceed the amount of the company's debt. This, he said, helps prevent excessive use of cross-claims to avoid winding up petitions.

143 See analogous cases on s 41(1) of the Bankruptcy Act 1966 (Cth). On hearing of a petition in bankruptcy proceedings a debtor can show he has a "counter-claim, set-off or cross-demand" that reduces the petitioner's debt below the amount required to support the petition: *Re A Debtor; Ex p Peak Hill Goldfield Ltd* [1909] 1 KB 430, 438; *Re Brink; Ex p the Commercial Banking Co of Sydney Ltd* (1980) 44 FLR 135.

144 [1954] VLR 505; [1954] ALR 917.

145 Per Barker J in *Universal Chemicals Ltd* v *Hayter*, supra n 142.

usually suffice as long as it has substantial grounds and is for a sufficient amount. The English Court of Appeal, to take a popular example, has given decisive weight to evidence of a cross-claim based on a cause of action that was unknown to English law but which existed under the Belgium Civil Code, and which was being pursued by the company in Belgium with "at least some chance of success".[146]

When can one say a company's dispute of indebtedness or cross-claim is based on substantial (or bona fide) grounds? Needham J says that the company must merely show that its defence is not "frivolous".[147] As noted above, Harman LJ in *Re LHF Wools Ltd,*[148] referring to a cross-claim, thought that "some chance of success" was substantial enough. Barker J in *Universal Chemicals Ltd* v *Hayter* spoke of "an arguable counter-claim".[149] Such formulations may seem rather favourable to the debtor company, but the consequences of premature liquidation arguably demand them. On these tests the company need not show it is likely to be successful in its dispute or cross-claim – there must only be some substance in its objection,[150] a possibility of success. It would be imposing a higher test to require the company to show it has a probability of success. However it seems a company seeking an injunction, for example to restrain presentation of a petition, may face this higher standard.[151]

Applications by the Commissioner of Taxation: What is the effect of a request for review of, or appeal against, assessment?

Winding up petitions or applications brought by the Commissioner for tax debts where the taxpayer company disputes the assessment are not uncommon. Can the company rely on a substantial dispute over the tax assessment as grounds for seeking a dismissal or suspension of the Commissioner's application?

Section 201 of the Income Tax Assessment Act 1936 (as amended) is at the heart of the matter:

> "The fact that an appeal or reference is pending shall not in the meantime interfere with or affect the assessment the subject of the appeal or reference; and income tax may be recovered on the assessment as if no appeal or reference were pending."

Does this mean that, although the taxpayer has applied for a review or appeal, the Commissioner can claim that such amount of the disputed assessment that remains unpaid is an overdue "debt" which can be the basis of a s 364 winding up order no matter what the substance of the taxpayer's objection? This was the claim the Commissioner made in two

146 *Re LHF Wools Ltd* [1970] 1 Ch 27, 37.

147 See *Re Damons Insurance Brokers Pty Ltd* [1979] ACLC 32,027, 32,030. He also used the phrase "frivolous or not substantial" in *GB White* v *Taylor Railtrack Pty Ltd* [1978] ACLC 30,100, 30,105.

148 [1970] 1 Ch 27, 37.

149 Unreported, Auckland Supreme Court (A1809/79, 7 March 1980).

150 Cf Roxburgh J, who in *Re A Debtor* [1958] 1 Ch 81, 99 (a case on the equivalent of s 40(1)(g) of the Bankruptcy Act 1966), when speaking of a cross demand against a judgment debt or sum payable under a final order, ruled: "But in my opinion a demand must be more than bona fide: the Court must be satisfied that it has a reasonable probability of success." See also *Ebert* v *The Union Trustee Co of Australia Ltd* (1960) 104 CLR 346, 350; and recently, *Re Brink; Ex parte the Commercial Banking Co of Sydney Ltd* (1980) 44 FLR 135, 140-141.

151 See supra n 59.

1976 cases; *Re Roma Industries Pty Ltd* [152] and *Fortuna Holdings Pty Ltd.*[153]

In the first the court noted that generally s 201 will cause the court to refuse to stay winding up petitions "Whatever the merits or demerits of the provision may be".[154] There the Commissioner alleged the company was indebted for approximately $36,000, comprising income tax, Division 7 tax, and additional tax and penalty because of late payment. A s 222 UCA demand was served on the company and this was not complied with. Acting within its rights under s 187 of the Income Tax Assessment Act 1936, the dissatisfied taxpayer requested the Commissioner to refer the matter to a Board of Review or treat the objection as an appeal and forward it to the Supreme Court. Even so Bowen CJ said the Commissioner, his standing assured, was "prima facie entitled to a winding up order".[155] Notwithstanding the appeal, the court ruled the amounts were "due and payable, and could be successfully sued for by the Commissioner in a court of competent jurisdiction; the existence of the appeal would not be a defence..." [156] Section 201 requires the court to treat the debt as in effect undisputed, Bowen CJ said, even though the results may be "unjust and even baneful".[157]

If Bowen CJ's judgment is taken at face value the assessment that may be the subject of soundly-based objection may itself render the company insolvent. The Commissioner has here potentially great power, and, one might argue, power that can but does not necessarily flow from the plain meaning of s 201. Certainly one may wonder whether or not such an impact of the provision in the winding up arena was intended by the legislature. The case for greater powers than usual for the Commissioner is not convincing. Why should the Commissioner carry such an advantage, especially when (until recently) he had a preferred position over at least unsecured creditors in distribution of assets in liquidation proceedings? [158] Why, when a reference to a Board of Review is requested or pending, should the Commissioner have power to recover tax assessments beyond those set out in s 209 of the Income Tax Assessment Act under which unpaid tax can be sued for in any court of competent jurisdiction, (especially as the court generally is, because of s 201 and related provisions, cautious about granting stays of

152 (1976) 76 ATC 4113; (1976) 1 ACLR 296.

153 [1976] ACLC 28,634; (1976) 76 ATC 4312; 6 ATR 620.

154 (1976) 76 ATC 4113, 4116 and 1 ACLR 296, 299 per Bowen CJ. His Honour cites *Marina Estates Pty Ltd* v *Deputy Commissioner of Taxation* (1976) 74 ATC 4166; 4 ATR 396 (which is probably misapplied: see *Re Norper Investments* (1977) 15 ALR 603, 606-607); and *Deputy Commissioner of Taxation (WA)* v *Australian Machinery & Investment Co Pty Ltd* (1945) 3 AITR 236.

155 (1976) 1 ACLR 296, 297.

156 Ibid. Bowen CJ cites *Deputy Commissioner of Taxation* v *Niblett* (1965) 83 WN (NSW) 405.

157 (1976) 1 ACLR 296, 299 citing Higgins J in *Hickman* v *Federal Commissioner of Taxation* (1922) 31 CLR 232, 245.

158 On 19 September 1980 Royal Assent was given to the Taxation Debts (Abolition of Crown Priority) Act 1980 which limits the Commissioner's preferential right to payment of taxes in company liquidations. Section 221 of the Assessment Act is repealed retrospectively from 1 November 1979 and the Commissioner's claims will be treated in winding up like those of any other unsecured creditor: secured and preferred creditors shall be paid in priority.

execution).[159] Why can the Commissioner not be required to settle for something short of winding up until the appeal is heard or debt adjudicated on — for example, by suing for the amount of the assessments, or extracting undertakings or security from the taxpayer, or seeking the appointment of a provisional liquidator to ensure that the company will not dispose of its assets otherwise than in the ordinary course of business,[160] or getting the taxpayer to pay a reasonable part of the assessment to demonstrate good faith? [161]

Is it enough to say that the Commissioner will only use this power with circumspection? Are there compelling reasons to believe that his motives will be sounder, that his need for payment is any greater, or that his ability to assess the state of the company's affairs is higher than those of competing creditors? Putting aside s 201, why should the Commissioner have greater powers than other creditors in winding up proceedings; why can he be both a doubtful creditor and, in effect, judge and jury on the existence of the debt? Other creditors must prove their debt beyond substantial dispute;[162] why not the Commissioner?

McGarvie J in *Fortuna Holdings Pty Ltd* [163] blunted the sharp edge of the *Roma Industries* decision. In a comprehensive judgment he conceded the relevance of the taxpayer's prospect of success in its objection to the assessment. Eight companies, all members of a group, had objected to their assessments. They all requested that their cases be referred to a Board of Review under s 187 of the Income Tax Assessment Act 1936. However the Commissioner served s 222 UCA demands on them all before their hearings. The companies unsuccessfully sought to restrain the Commissioner from commencing winding up proceedings. McGarvie J affirmed that the Commissioner did have the right to present a winding up petition for an unpaid tax "debt", that the provisions of the Assessment Act placed his standing beyond dispute, and that failure to pay an assessment, even one subject to reference or appeal, amounts to "neglect" within s 222(2)(a). But, citing a judgment of the majority of the High Court in *DC of T(WA)* v *Australian Machinery and Investment Co Pty Ltd,*[164] McGarvie J found that, while the mere existence of a reference to the Board or an appeal of itself does not affect the Commissioner's right to payment of assessed tax, s 201 does not virtually compel the court to refuse a stay:

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159 See position discussed by Castan, "Enforcement of Payment in Contested Tax Cases" (1976) 5 Australian Tax Review 4. See also McGarvie J in *Fortuna Holdings Pty Ltd* v *FC of T* [1976] ACLC 28,634, 28,647-28,648. In *DFC of T* v *Bevz* (1981) 81 ATC 4,185 the court refused a stay of execution where the possibility of extinction or reduction of the tax debt in the pending reference to the Board was "remote".

160 As in *DC of T (WA)* v *Australian Machinery and Investment Co Ltd* (1945) 3 AITR 236.

161 Evatt J in *Federal Commissioner of Taxation* v *Trautwein* (1936) 56 CLR 211 stayed proceedings in the Commissioner's action by writ for £162,826 upon the defendant's undertaking to pay £5,000 and facilitate the hearing of the appeals.

162 The usual position with creditors is put by Needham J in *Medi Services International Pty Ltd* v *Jason Pty Ltd* (1978) 3 ACLR 518: "If petitions are filed by parties who have not established their claims, either by admission or process of law, and if the respondent to that petition seeks relief on the basis of a bona fide dispute, it is I think for the petitioner to show plainly and without doubt, on a balance of probability, that there is no substance in the alleged dispute which the respondent to the petition asserts." This passage was cited by Kearney J in *Re Field Group Chemicals Pty Ltd*, unreported, NSW Supreme Ct (No 2352, 19 August 1980).

163 [1976] ACLC 28,634; (1976) 76 ATC 4312; 6 ATR 620.

164 (1945) 8 ATD 133; 47 WALR 9.

> "...while the policy stated in s 201 is a consideration to which great weight should be attached, other considerations, *including the extent of the taxpayer's prospect of success in an appeal or reference,* can justify the exercise of discretion in a way which delays the Commissioner's recovery." [Emphasis added].[165]

His Honour distinguished *Re Roma Industries* on the basis that there the company hoped the mere existence of pending references converted the debts into doubtful debts. There, he stressed, the company made no attempt to show the appeal to the Board was based on substantial grounds; certainly a material point of difference. A dispute must be substantiated and not merely alleged:[166] otherwise how can the court decide if the dispute has substance or not? [167]

In *Fortuna Holdings,* though, three of the companies did satisfy the court that their appeals to the Board were based on substantial grounds. But they did not get their injunction because they were largely dormant and the court was not satisfied there was any real risk of damage (beyond that they would suffer anyway because of presentation against the other five companies) sufficient to warrant the court restraining presentation. McGarvie J thought that only if the damage likely to be caused by advertisement was at least "significant and substantial" could the court interfere.[168] This decision for these three companies was harsh. Other creditors without the support of a provision like s 201 cannot negate or even minimise the force of arguments against their standing simply by showing the prosecution of the claims (as yet insufficiently proved) would have little deleterious effect on the debtor.

Bowen CJ in *Re Roma Industries* was not purporting to lay down an absolute rule that s 201 means that in *all* cases the court will refuse a stay or dismissal. He said that "the Commissioner will *generally* be entitled to a winding up order notwithstanding that appeal has been lodged and has not been heard..." [169] [Emphasis added]. McGarvie J in *Fortuna Holdings* felt this was insufficient concession. He concluded that the authorities suggested, "the particular circumstances of cases involving

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165 [1976] ACLC 28,634, 28,646-28,647.

166 See, eg, *Re KL Tractors Ltd* [1954] VLR 505, 509 per O'Bryan J: "It is not enough to show simply that the company believes it has a defence or a set-off or even that it has obtained leave to defend the action for enforcement of its alleged debt (see *Re Welsh Brick Industries Ltd* [1946] 2 All E.R. 197)." See also *Re Douglas (Griggs) Engineering Ltd* [1962] 1 All ER 498.

167 Accordingly the alternative basis of Slade J's recent decision in *Re Laceward Ltd* [1981] 1 WLR 133 is of interest. One of his grounds for dismissing a petition was that, because the solicitor's costs for non-contentious business there at issue had not been taxed, the true sum due was not known and thus there was substantial dispute as to the existence of the debt, and thus as to the petitioner's locus standi. The request by the company for taxation was not made until after the petition was presented, and the company had conceded that "almost certainly" some money was due. How, then, can it be said that the petitioner lacked standing? Slade J also does not say whether or not the company's grounds for seeking taxation of costs are substantial. He simply says at 137:

> "Before such taxation [of costs] takes place there is no certainty whatever as to whether all or any specific part of the debt alleged by the petition will be found truly due to the petitioners".

168 [1976] ACLC 28,634, 28,655, citing *Charles Forte Investments Ltd* v *Amanda* [1964] 1 Ch 240, 257-258.

169 (1976) 1 ACLR 296, 299.

s 201 lead courts sometimes to grant and sometimes to refuse a stay, rather than that the section generally leads a court to refuse a stay." [170]

McGarvie J ruled that the latitude allowed a disputing taxpayer company ends with an unfavourable decision of a Board of Review (or, of course, of a Supreme Court). Then the Commissioner can present his application unhindered.[171] This seems reasonable, and one may question the force of warnings, such as that noted by Bowen CJ in *Re Roma Industries,*[172] that recalcitrant taxpayers may withhold payment and use their money to conduct ill-based appeals against the Commissioner.[173] Aside from the fact that such an observation if it comes from the applicant must carry little weight, it offers a rather unlikely scenario — a company in its death throes using its last resources up in litigation costs and expenses simply to deny the Commissioner the satisfaction of collecting taxes. That is as unlikely as the other possibility; that the Commissioner would deliberately use the threat of winding up to extract payment from a struggling company and thereby inhibit its ability to fund an effective appeal.

The most recent Australian case in this area is *Re Norper Investments Pty Ltd.*[174] There Needham J endorsed McGarvie J's approach. He said:

> "I have no doubt that, despite the provisions of s 201, the Court has a general discretion to grant a stay of proceedings." [175]

Needham J acknowledged that s 201 "must be taken into account in considering whether a stay should be granted".[176] But, he added, if the company presents substantial objections to the assessment and it is possible that the whole amount of the assessment will be set aside on appeal then a stay could be granted, and without any other terms being imposed (such as, for example, part payment of the assessment). If substantial argument is shown to the effect that the assessment is excessive, then on payment of the undisputed portion a stay could similarly be ordered. Thus Needham J favoured the view that the court retains a flexible discretion to grant a stay of proceedings to await adjudication by the Board or to dismiss a Commissioner's petition or application on the ground that an assessment could be set aside in a pending appeal.

The facts of *Norper Investments* justified some of the fears that critics of the dicta in *Roma Industries* felt. Norper Investments Pty Ltd was assessed to Division 7 tax under the Income Tax Assessment Act. It had distributed a large amount of its taxable income as dividends on preference shares issued to another company. A previous Board of

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170 [1976] ACLC 28,634, 28,648.

171 Ibid 28,649.

172 (1976) 1 ACLR 296, 299: "It must be appreciated that from the point of view of the revenue it is a protection against that class of taxpayer who might withhold payment and use the money as the sinews of war to conduct appeals against the Commissioner and who, being finally unsuccessful, was found to be unable to meet his tax liability, having spent his money on the litigation."

173 A similar sort of argument was referred to, in a different context, by Harman LJ in *Re LHF Wools Ltd* [1970] 1 Ch 27, 37-38.

174 (1977) 15 ALR 603; [1977] ACLC 29,427.

175 Ibid 607 and 29,430 respectively. The Australian Law Reports version at 607 rather unfortunately omits the word "no" before "doubt" in this passage.

176 Ibid.

Review decision,[177] on facts on all fours with those at issue here, had held that the method the company here used to distribute this income, ie the declaration of dividend, was not void under s 260 of the Income Tax Assessment Act. However the Commissioner went ahead, asserted that s 260 required him to ignore the dividend paid on shares the second company held, and assessed that amount to tax. The company did not pay the assessment upon the Commissioner's demand notice.

Meantime over a year had elapsed and still the Commissioner had not complied with his mandatory duty under s 188 of the Income Tax Assessment Act to forward the company's objection to the Supreme Court. As Needham J pointed out, it was ironic that the Commissioner "sought to convince the Court that he was entitled to a winding up order because of other provisions of the Statute he was studiously breaching." [178] He sought to use s 201 but ignore s 188. His Honour dismissed the petition as vexatious, oppressive and an abuse of process.[179]

Conclusion

One area of possible concern is recent judicial comment upon the precise meaning and impact of s 222(2)(a) UCA [s 364(2)(a)]. A finding that any notice specifying a sum different from the amount in fact due is invalid would affect the usefulness of this method for determining statutory insolvency. Inventive debtors, one imagines, could relatively easily produce doubts about the quantum of the debt demanded in the hope of rendering the demand invalid.

The legislation calls for the creditor to prove merely that at least $1,000 [$100 in UCA] is presently due and payable. And once an order is granted then the successful applicant, like the other creditors, must prove his debt, and the company's assets are distributed as far as they extend. Does it matter that the wrong sum is demanded, providing the minimum indebtedness is established beyond substantial dispute or cross-claims? There is no indication in the wording that the legislature intended a narrow interpretation of paragraph (a). If the controversy continues and the court imposes a narrow interpretation of the provision then the legislature may be urged to consider introducing provisions such as those in bankruptcy law dealing with overstated and understated demands.

A matter of minor interest is the substitution in s 364(2)(a) of the word "failed" for the former "neglected". Although the dictionary meaning of the words is different, and although a series of decisions has relied on an acknowledged although narrow meaning of "neglected" in the context of the provision, the court will no doubt adopt a special meaning for "failed" as it is used in s 364(2)(a) NCA and forestall any problems the change may invite.

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177 *Case H 53* (1976) 76 ATC 451; *Case 22* 21 CTBR (NS) 212. The Board there applied the High Court decision in *Mullens* v *Federal Commissioner of Taxation* (1976) 10 ALR 513; 76 ATC 4288.

178 (1977) 15 ALR 603, 608; [1977] ACLC 29,427, 29,430-29,431.

179 *Norper Investments* was noted by Lush J in *Commonwealth of Aust* v *Duncan* [1981] VR 879, 883; (1981) 81 ATC 4,228, 4,231-4,232: "...[*Norper*] merely illustrated the power of the court to reject a winding up petition, even if the petitioner's debt is proved, if the petition is regarded as oppressive or as an abuse of process."

Recently the court has forthrightly restated what great damage a company can suffer on the mere presentation and advertisement of a winding up application. Public trading companies are particularly vulnerable, but all companies that rely to some extent on public confidence and reputation are at risk. And the over-zealous creditor knows it. The court is willing enough to grant injunctions to restrain presentation. McGarvie J in his frequently-cited judgment in *Fortuna Holdings* defined preconditions for the granting of injunctions in such circumstances. His careful judgment compares well with that of Ungoed-Thomas J in *Mann* v *Goldstein.*

The term "bona fide", when used in reference both to the creditor's purpose in seeking a winding up order, and to the adequacy of a company's dispute of indebtedness or its cross-claim, may have outlived its usefulness, if it ever had any. The one word — "substantial" — serves the purpose in the second context and its meaning is clear. Notions of fair play, genuineness and lack of ulterior motive that the words "bona fide" connote in the first context arguably are irrelevant in the often combative arena of creditors' petitions. Suffice to say that whenever emotive terms such as "blackmail", "scandalous abuse" and "sinister objects" appear in a judgment in condemnation of a petitioner's motives, some other more tangible reason for the rejection or staying of the petition or the issuing of an injunction is also given; lack of standing in the petitioner being the most common. This writer has not found one case where an ulterior motive — ie a motive other than that of getting paid — in a petitioning creditor was the sole or major ground for his lack of success. In the interests of clarification of the issues facing the court it could ignore a creditor's motives and concentrate on the objective issues — has the creditor standing, have the procedures been faithfully followed, and is there a substantial dispute or cross-claim?

The Commissioner of Taxation's position is, probably accidentally, a privileged one in the winding up arena. Section 201 of the Assessment Act assures him of standing, and failure to pay a disputed assessment is "neglect" within s 222(2)(a) UCA, even where a taxpayer has sound or substantial grounds for disputing the assessment. However the court has reminded the Commissioner of its power to issue injunctions and to grant, stay or dismiss applications. It will not grant an order where the Commissioner's application is oppressive, vexatious and an abuse of process, notably where it thinks the assessment on appeal will be set aside in whole or in part (providing in the latter case that the company pays the undisputed portion). It may issue an injunction to prevent presentation or advertisement where it thinks the presentation might produce irreparable damage to the company and where some suitable alternative procedure for recovering the debt is open to the Commissioner.

While there are areas of uncertainty in the law on compulsory winding up of companies for insolvency, the overall position seems sound enough. The new legislation makes few changes and, it seems, none of real significance. The lack of change indicates an endorsement of the manner of the court's exercise of its discretion.