

Creditor Alert - A Reminder of the Ability to Unwind Transactions Outside the Insolvency Regime

Millie Teh | March 2015 | Commercial Disputes & Transactions

Summary

Creditors will be well aware of the provisions of the *Corporations Act 2001* (Cth) ('**Corporations Act**') and the *Bankruptcy Act 1969* (Cth) ('**Bankruptcy Act**') giving liquidators and trustees powers to unwind transfers of property that have been undertaken either at an undervalue or to defeat creditors or create a preference for a creditor over other creditors.

There is another method which does not require the insolvency and bankruptcy of a debtor which may cause inconvenience to the debtor and promote payment of a debt.

Creditors should be aware of section 37A of the *Conveyancing Act 1919* (NSW) ('**s37A**') which provides a similar mechanism for ordinary creditors to claw back property. However, unlike the Corporations Act and the Bankruptcy Act, debtors are not required to be insolvent or bankrupt for an application under s37A to be successful. This means that creditors can personally bring an action under s37A (rather than through a liquidator or trustee) to have the court declare the transaction voidable and the property returned to the original owner for the purpose of satisfying the debt owed to the creditor.

Who does this impact?

All creditors (including future, prospective and contingent creditors) where the debtor has knowledge of the existence of the relevant creditor and transfers property with intent to defraud creditors. Accordingly, future creditors with an impending liability may also make an application under s37A.

Legislative provision

S37A states that '*every alienation of property... with intent to defraud creditors, shall be voidable at the instance of any person thereby prejudiced*'. The section goes on to say that it '*does not extend to any estate or interest in property alienated to a purchaser in good faith not having, at the time of the alienation, notice of the intent to defraud creditors*'.

Equivalent provisions exist in the legislation of all other Australian States.

Time limitations

With the exception of the Crown, all s37A applications must be commenced within twelve years from the date of the relevant property transfer (s 27(2) of the *Limitation Act 1969* (NSW)).

Process

All s37A applications are required to be commenced by way of court application.

Recent case law

A 2014 case serves as a timely reminder not only of the ability of creditors to utilise s37A but also that it can be a useful and effective tool for current and prospective judgment creditors who seek to recover their judgment, costs orders or both but have fears that the debtor(s) may have insufficient funds to pay.

In *Bowden v Weldon* [2014] NSWSC 109 (**'Bowden'**), the Supreme Court of NSW set aside the transfer of a property in Lilyfield by the first defendant to the second defendant on the basis that it was made with the intent to defraud creditors. The property comprised a home unit in a block of units.

By way of background, the first defendant had assaulted the plaintiff. The plaintiff was in the process of suing the first defendant for damages as a consequence of that assault. Before those proceedings were finalised, the first defendant, while incarcerated, transferred his home unit to the second defendant. The transfer acknowledged receipt of \$245,000 as consideration for the transfer. The contract records that the sale was effected "*without the intervention of an agent*" and without the payment of a deposit. The contract also records that the sale was subject to existing tenancies rather than a sale with vacant possession of the land.

On the evidence before the Court:

- No monies changed hands for the sale of the property. There was no record, in the first defendant's banking records, of any receipt of monies that could, objectively, be characterised as sale proceeds.
- There was an agreement between the first defendant and the second defendant that the parties would share future rent derived from letting the property out to tenants.
- The second defendant was the mother-in-law of an inmate in the same jail as the first defendant.

The Court held that the transfer was not a bona fide transaction but rather an arrangement made for the continuing benefit of the first defendant. The object of the transaction appears, objectively, to have been to transfer the land out of the name of the first defendant in order to defeat or delay any entitlement to compensation that the plaintiff might have had, or might soon obtain (as she did obtain) in court proceedings, against the first defendant arising out of his assault upon her on 21 April 2010.

The Court ordered that the property be retransferred to the first defendant and that the first defendant and second defendant not deal with the property without prior leave of the Court.

Conclusion

S37A is an alternative means of recovering property from a debtor. Consequently, if a debtor has knowledge of a creditor and the debtor transfers property to another person who has knowledge of the existence of the creditor, and it can be established that the transaction was done in any way to defraud, hinder or delay a creditor, then the court can declare the transaction voidable and the property returned to the original owner for the purpose of satisfying the debt owed to the creditor.

S37A can be a very effective tool for creditors to claw back property from debtors outside of an insolvency and bankruptcy regime for the purpose of recovering the debts owed to them. And as *Bowden* has shown, this is especially so for judgment creditors and impending judgment creditors.

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