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Assigning the right to sue – the new provisions'

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External administrators of companies can now assign any right to sue that is conferred on them by the Corporations Act, for example voidable transaction claims and insolvent trading claims. Previously these were considered rights that could only be utilised by the appointed liquidator and so could not be assigned. Now they can.

Thomas Russell, **Partner** and **Brendan May**, **Lawyer** discuss these new changes and what they mean for insolvency practitioners.

When did this start?

- This has already begun. It commenced on 1 March 2017.

What legislation brought this about?

- The *Insolvency Law Reform Act 2016* (Cth) has introduced a new schedule to the *Corporations Act 2001* (Cth). The schedule is called "*Schedule 2 – Insolvency Practice Schedule (Corporations)*"(**the Schedule**).
- The external administrator is able to assign his or her right to sue under section 100-5 of the Schedule.
- The *Bankruptcy Act 1966* (Cth) now also has a Schedule 2 called "*Schedule 2 – Insolvency Practice Schedule (Corporations)*. Section 100-5 similarly provides that any right to sue conferred upon a trustee of a debtor's estate (including a bankrupt estate) can be assigned.

How does it happen?

- In the usual way anything is assigned, for example by Deed of Assignment. The right is broad, and – subject to one or two things – allows the external administrator to assign "*any right to sue that is conferred on the external administrator by this Act*".
- The conditions are these:
    - if the external administrator's action has already begun, the external administrator cannot assign the right to sue without the approval of the Court;
    - before assigning any right to sue, the external administrator must give written notice to the creditors of the proposed assignment; and
    - once assignment has been effected, a notice of assignment must be issued that complies with s 12 of the *Conveyancing Act 1919* (NSW). Note this is a piece of New South Wales legislation, however there are equivalent provisions in other state legislation.
- Note that depending on its terms, the assignment may be captured by s 477(2A) or (2B) and require approval of creditors or the Court before it is entered into:
    - if the right is assigned pursuant to an arrangement that will extend for more than three months, for instance an assignment in exchange for, among other consideration, an uplift or success fee upon the entry of judgment or recovery of monies; or
    - if the right being assigned is a debt due to the company (for instance a right to recover compensation for insolvent trading) and the circumstances of the assignment are such that this "debt" is effectively being compromised. There is (for obvious reasons) yet to be any case law on this situation but liquidators would be

well advised to play it safe.

Who does this apply to?

- It applies to "External Administrators". This is defined in item 5-20 of the Schedule:

5-20 Meaning of external administrator of a company

A person is an external administrator of a company if the person is:

(a) the **administrator of the company**; or

(b) the **administrator under a deed of company arrangement** that has been entered into in relation to the company; or

(c) the **liquidator of the company**; or

(d) the **provisional liquidator** of the company.

Note: A person is not an external administrator of a company for the purposes of this Schedule merely because the person has been appointed as a receiver, receiver and manager, or controller in relation to property of the company.

Why could this not happen before?

- The simple reason it couldn't happen before is that people tried it, and the Courts said it couldn't be done.
- A right to sue is known as a *chose in action*. The **common law** had long held a distrust of assignment of choses in action. However **equity** permitted it to happen, and over time it became accepted. However, the ability to assign a chose in action has always been the exception, rather than the rule.
- The law has also had a historical wariness of "champerty" and "maintenance" – allowing a third party to meddle in and/or to profit off litigation. They used to be crimes and "torts" (unlawful acts).
- Voidable transaction claims, or insolvent trading claims, are all *choses in action* that are conferred personally on the external administrator by statute. When assignments of these were attempted in the past, Courts had regard to the historical context and the language of the section, e.g.
    - section 588M (insolvent trading) the statute provides "The company's liquidator may recover from the director, as a debt due to the company, an amount equal to the amount of the loss or damage", or
    - section 588FF (voidable transactions) provides "Where, on the application of a company's liquidator, a court is satisfied that a transaction is voidable…"

…and said that the statute says only a liquidator can bring the action, so we won't let the liquidator assign it to someone else.

- This has now changed.

What could an external administrator already assign before these provisions?

- A liquidator of a company could (and still can) sell or otherwise dispose of, in any manner, property of the company pursuant to section 477(2)(c).
- Common law rights of action, vesting in the liquidator, are considered to be property of the company. So an external administrator always had a right at common law to assign debts, and some other causes of action which we will discuss shortly.
- Likewise, straight-up debts (such as trading debts due by customers of the company) are, and always have been, assignable.
- The only condition with debts and other legal actions is that notice of the assignment must be given to the debtor in order to effect a legal assignment pursuant to section 12 of the *Conveyancing Act 1919* (NSW). Without this, it is only an "equitable assignment", that is, a partly-completed assignment that still needs to be completed by compliance with the correct legal procedure.
- Note that there is a general principle that claims for misleading and deceptive conduct cannot be assigned. The reason is that the relevant statutory provision giving a right to damages for loss suffered as a result of a breach (section 82 of the TPA, now section 236 of the Australian Consumer Law) does not provide for the award of damages in respect of a loss suffered by another, i.e. one that was not suffered by any party to the proceedings: *Boston Commercial Services Pty Ltd v GE Capital Finance Australasia Pty Ltd* [2006] FCA 1352.

- The good news is that there is a line of authority, including in NSW (*CBD Prestige Property Holdings No 3 Pty Ltd v Metropolitan Local Aboriginal Land Council* [2013] NSWSC 1005), that suggests a liquidator is a special exception to the general principle above. The bad news is that this is in conflict with other authority from other states and at federal level on the same point, meaning that the position is not settled as far as the law is concerned.
- If you are ever required to consider whether or not you are able to assign a claim for damages for misleading and deceptive conduct, specific legal advice should be sought and your advisor's attention should be drawn to the two cases mentioned above.

What's the big deal about notice and the *Conveyancing Act*?

- In NSW, assignments of debts and choses in action are governed by section 12 of the Conveyancing Act. This provides that there is four criteria that must be met in order to effect a legal assignment:
    - It must be an absolute assignment (so you cannot legally assign part of something, e.g. half a bank account if it was a debt);
    - It must be in writing;
    - It must be signed by the assignor; and
    - Written notice must be given to the debtor or potential defendant. Note that the written notice has to come *after* the assignment, and it does not matter whether written notice comes from the assignor or the assignee, as long as somebody tells them 'The right, title and interest to the claim against you has been assigned by *x* to *y*'.

What happens if notice is not given?

- If notice is not given, you only have an equitable assignment, not a legal assignment.
- This means legal title to that claim has not actually passed – only that (provided consideration has been paid) equity will treat it that it should have been passed. So the assignor technically retains legal title to the action, while the assignee has equitable title. The assignee can sue on the claim, but a rule of practice and procedure requires the assignor to be a party to the action.
- If the assignor is not joined in such an action, there are decisions (see *Jennings v Credit Corp Australia Pty Ltd As Assignee From Citicorp Person To Person Financial Services Pty Ltd* [2000] NSWSC 210) which have held that until the legal assignor is joined or notice given, the equitable assignee cannot recover under the claim. The easiest way if notice hasn't been given but proceedings have commenced is just to give notice. It is then perfected into a legal assignment and will operate retrospectively.
- An equitable assignment is also susceptible of being defeated by other principles of equity (for example, if the equitable assignee does not come to court with 'clean hands').

Who will be interested in purchasing these claims?

- Litigation funders would seem to be the most obvious market for these claims.
- Other potential purchasers would be related parties, who may have an interest in:
    - controlling the vote at a meeting of creditors (see Rule 75-110(4) of the bankruptcy IPRs re valuation of assigned claims, but note that no equivalent rule exists for corporations); or
    - ensuring the claim is under the control of a friendly party, for asset protection reasons or to obtain a tax benefit.

Should you have any questions, please contact either Thomas Russell or Brendan May.