Banking & Financial Services Law Association Conference 29 August 2016

Judicial Case Law Update - Australia

Justice Ashley Black

Supreme Court of New South Wales

I will spend about half of the paper on dealing with recent developments in respect of penalties, most importantly the High Court's decision in *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28 ("*Paciocco HCA*"), although I will also refer briefly to English and New Zealand case law in respect of penalties. I will also deal with several other developments in insolvency law relevant to banking and financial law and practice and also touch upon forthcoming legislative change, by way of the Insolvency Law Reform Act and the suggested introduction of a safe harbour from liability for insolvent trading liability.

The concept of a penalty

The several decisions to which I will refer generally refer to the several propositions identified by Lord Dunedin in *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, as follows:

> "1. Though the parties to a contract who use the words "penalty" or "liquidated damages" may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages. This doctrine may be said to be found passim in nearly every case.
>
> 2. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage …
>
> 3. The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach …
>
> 4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:
>
> (a) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach…
>
> (b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid … This though one of the most ancient instances is truly a corollary to the last test…

(c) There is a presumption (but no more) that it is penalty when "a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage" …

On the other hand:

(d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties…" [citations of authority omitted]

The concept of a penalty was subsequently described in *Legione v Hateley* (1983) 152 CLR 406 at 445; [1983] HCA 11 by Mason and Deane JJ as "in the nature of a punishment for non-observance of a contractual stipulation" involving "the imposition of an additional or different liability upon breach of the contractual stipulation". In *Ringrow Pty Ltd v BP Australia Pty Ltd* (2005) 224 CLR 656 at 662; [2005] HCA 71 a unanimous High Court in turn observed that:

> "The law of penalties in its standard application is attracted where a contract stipulates that on breach the contract-breaker will pay an agreed sum which exceeds what can be regarded as a genuine pre-estimate of the damage likely to be caused by the breach."

The Court also there observed (at 667–669) that the unenforceability of a penalty required that the stipulation applicable on breach was "extravagant and unconscionable in amount" or "out of all proportion" by comparison to a genuine pre-estimate of damages. The description of a penalty in *Legione v Hateley* above was quoted with approval by the High Court in *Andrews v Australia and New Zealand Banking Group Ltd* (2012) 247 CLR 205; (2012) 290 ALR 595; [2012] HCA 30 *("Andrews HCA")* at [9], by Lord Neuberger and Lord Sumption in *Cavendish Square Holding BV v Makdessi; Parking Eye Ltd v Beavis* [2015] 3 WLR 1373; [2015] UKSC 67 at [31] and by Kiefel J in *Paciocco HCA* at [32].

The Andrews proceedings

The history of the bank fee litigation is, of course, well known, and there have been suggestions that the proceedings commenced against several banks in Australia and New Zealand would be paralleled by proceedings against other financial services providers and possibly against utilities and other service providers that charge fees in respect of late payments. The proceedings, of course, involved several forms of bank fees, including fees described as "honour", "dishonour" and "non-payment fees" charged for consumer and business deposit accounts and "over-limit" and "late payment" fees for credit card accounts.[1] The applicants claimed that the relevant fees were unenforceable

[1] "Honour" and "dishonour" fees were charged when ANZ made or declined to make a payment on a customer's behalf where that customer had insufficient funds; "over-limit" fees were charged where a customer exceeded its credit limit on a credit card account; "non-payment" fees were charged where a periodic payment was not made because of insufficient funds in an account; and "late payment fees" were

as contractual penalties and also brought statutory claims for unconscionable conduct under the *Australian Securities and Investments Commission Act* 2001 (Cth) and the then *Fair Trading Act* 1999 (Vic), under the unfair term provisions in the *Fair Trading Act* and under the unjust transaction provisions under the *National Credit Code*. The challenge to these fees paralleled a challenge which had previously been brought, unsuccessfully, in the United Kingdom.[2] I will deal with the decisions in Australia, the United Kingdom and New Zealand in chronological order, since the later decisions are plainly influenced by decisions in the other jurisdictions.

The proceedings at first instance in *Andrews v Australia and New Zealand Banking Group Ltd* (2011) 211 FCR 53; (2011) 288 ALR 611; [2011] FCA 1376 ("*Andrews FCA*") and on appeal in *Andrews HCA* were directed to separate questions as to whether the relevant fees were payable on breach of contract by a customer, or on the occurrence of an event constituting a default under the contract which the customer was obliged to avoid, and whether they should be characterised as penalties. In *Andrews FCA,* Gordon J held, at first instance, that only the late payment fees in respect of credit cards were payable on breach of contract, and accordingly only those fees were within the scope of the penalty principle. Her Honour there followed the decision of the Court of Appeal of the Supreme Court of New South Wales in *Interstar Wholesale Finance Pty Ltd v Integral Homes Pty Ltd* (2008) 257 ALR 292 [2008] NSWCA 310, which had held that the penalty principle was only engaged where a contractual obligation was breached, and which was overruled in *Andrews HCA*.

The appeal from the first instance decision in *Andrews FCA* was removed from the Full Court of the Federal Court of Australia to the High Court under s 40 of the *Judiciary Act* 1903 (Cth). As is now well-known, the High Court held in a joint judgment in *Andrews HCA* that a stipulation can be a penalty although it is not triggered by a breach of contract. That approach was reflected in a wider description of the concept of penalty in that case (at [10]) as follows:

> "In general terms, a stipulation *prima facie* imposes a penalty on a party ("the first party") if, as a matter of substance, it is collateral (or accessory) to a primary stipulation in favour of a second party and this collateral stipulation, upon the failure of a primary stipulation, imposes upon the first party an additional detriment, the penalty, to the benefit of the second party. In that sense, the collateral or accessory stipulation is described as being in the nature of a security for and *in terrorem* of the satisfaction of the primary stipulation. If compensation can be made to the second party for the prejudice suffered by the failure of the primary stipulation, the collateral stipulation and the penalty are enforced only to the extent of that compensation. The first party is relieved to that degree from liability to satisfy the collateral stipulation."

The High Court's decision went no further than to indicate that the fees charged by ANZ could potentially be within the scope of the penalty principle, although they were not

---

charged where a customer did not pay a minimum payment due on a credit card account on a specified date.

[2] *Office of Fair Trading v Abbey National Plc* [2008] 2 All ER (Comm) 625; [2008] EWHC 875 (Comm) and, on appeal, [2010] 1 AC 696; [2009] UKSC 6.

payable on breach of contract. That approach was not welcomed by all commentators.[3] Subsequent Australian case law has recognised that the High Court's decision did not affect the conventional approach that permitted the specification of a higher interest rate payable in the event of default in a loan contract.[4]

The Paciocco proceedings at first instance

A substantially similar claim in respect of the same range of fees was subsequently brought in *Paciocco v Australia and New Zealand Banking Group Ltd* (2014) 309 ALR 249; 2014; FCA 35 ("*Paciocco FCA*"). Mr Paciocco held a consumer deposit account and two consumer credit accounts and a company associated with him, Speedy Development Group Pty Ltd, held a business deposit account with ANZ. Mr Paciocco and Speedy Development Group had incurred the range of fees in issue in respect of those accounts. The applicants contended that those fees were penalties in contract and in equity, and also that they breached the statutory prohibitions that had been in issue in *Andrews*.

Gordon J there set out (at [15]) an approach that might be applied in determining whether a provision was a penalty which involved identifying (1) the terms and circumstances of the contract, judged at the time it was made; (2) the transaction that gives rise to the imposition of the relevant stipulation; (3) whether the relevant stipulation was payable on breach of contract, which was necessary to establish a penalty in law but not in equity; (4) whether, in substance, the stipulation was collateral to a primary stipulation in favour of one party and, on failure of that primary stipulation, it imposed an additional detriment on the other party in the nature of security for, or in terrorem of, satisfaction of the primary stipulation, so that it could constitute a penalty in equity; (5) if the third or fourth steps were satisfied, so that a penalty could potentially be established in law or equity, whether the stipulated sum was a genuine pre-estimate of damage or, alternatively, was extravagant or unconscionable in comparison with the greatest loss that could conceivably be proved and, if so, the sum stipulated would be unenforceable to the extent that it exceeded that greatest loss. That approach involves a clear distinction between the approach in law and in equity, consistent with the decision in *Andrews HCA*, and it contrasts a genuine pre-estimate of damage, on the one hand, with a penalty on the other, drawing upon the reasoning in *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* above.

Gordon J held that the fees, other than the late payment fee payable in respect of credit cards were not triggered by a breach of contract or a failure of a primary stipulation, and were fees for additional services requested by ANZ's customer, and could not be characterised as penalties, and also did not give rise to a breach of the relevant statutory provisions. Turning now to the late payment fees in respect of credit cards, ANZ accepted

---

[3] For commentary see B Taylor, "The High Court's Expansion of the Doctrine of Penalties in ANZ Banking Group" (2013) *Australian Banking and Finance Law Bulletin*, 106–110; PS Davies & PG Turner, "Relief against Penalties without a breach of Contract" (2013) *Cambridge LJ* 20; JW Carter et al, "Contractual Penalties: Resurrecting the Equitable Jurisdiction" (2013) 30 *Journal of Contract Law* 99.

[4] *Kellas-Sharpe v PSAL Ltd* [2013] 2 Qd R 233; [2012] QCA 37; *PT Thiess Contractors Indonesia v PT Arutmin Indonesia* [2015] QSC 123 at [151]–[157]; *Re Funds in Court; Application of Mango Credit Pty Ltd* [2016] NSWSC 199 at [89] (noting a possible distinction if the lower rate of interest was payable up front and the higher rate of interest applied only in the event of a subsequent default).

on the pleadings that these were not set by reference to a pre-estimate of the loss that ANZ would suffer by a delay in making the specified minimum payments. It was nonetheless necessary for the applicants to establish, and ANZ contested, that the amount of those fees was extravagant or unconscionable by comparison with the loss or damage that ANZ would or might sustain by a breach of the relevant contractual term or primary stipulation requiring payment of the minimum payment by a specified date. The basis on which that issue was to be determined was a critical issue in the subsequent appeal.

Gordon J accepted the applicants' expert accounting evidence as to the costs that were in fact incurred by ANZ in respect of late payments and did not include several categories of cost on which ANZ had relied. Her Honour held that the amount of the fee was not justified by reference to loss provision costs, which ANZ took to account in its profit and loss account to recognise the risk of future default by customers that were late in paying the minimum amount due, regulatory capital costs incurred by ANZ in holding additional capital by reason of late payments and fixed costs incurred in respect of its collection activities. Her Honour estimated the value of the relevant loss suffered by ANZ as $3.00, which was substantially less than either the initial, or a subsequently reduced, level of the late payment fee. Her Honour held (at [182]–[183]) that the late payment fees in respect of credit cards were "security for, or in terrorem of, the satisfaction of the primary stipulation" to make the minimum payment within the specified period and that the amount charged was extravagant and unconscionable so as to constitute a penalty at common law (consistent with her previous holding in *Andrews FCA*) and in equity. Her Honour did not need to address the statutory claims in respect of those fees. Her Honour summarised her findings (at [373]) as having effect that:

> "The liability to pay the late payment fee was payable on breach and further and alternatively, was collateral (or accessory) to a primary stipulation (to make payment by a particular date) in favour of ANZ. That collateral stipulation, upon failure of the primary stipulation, imposed upon the customer an additional detriment in the nature of a security for, and *in terrorem* of, the satisfaction of the primary stipulation which was extravagant, exorbitant, and unconscionable."

The Paciocco proceedings in the Full Court

On appeal in *Paciocco v Australia and New Zealand Banking Group Ltd* (2015) 236 FCR 199; (2015) 321 ALR 584; [2015] FCAFC 50 ("*Paciocco FCAFC*"), the Full Court of the Federal Court upheld Gordon J's findings that the fees other than the late payment fee for credit cards were not penalties and did not contravene the statutory provisions. The Full Court held that the late payment fees for credit cards were also not penalties in contract or in equity and then determined a matter which Gordon J had not needed to decide, that they also did not contravene the relevant statutory provisions.

Allsop CJ (with whom Besanko and Middleton JJ agreed[5]) observed that a two stage approach was necessary, involving (at [96]) first an inquiry whether a stipulation is security for a primary stipulation and imposes an additional detriment that is "out of all

[5] Besanko J also dealt with a limitations point

proportion to the loss suffered by the obligee" or is "inordinate, extravagant or oppressive", having regard (at [114]) to "the extent of the legitimate interest of the obligee in the performance of the relevant portion of the contract"; and, second, if the provision is a penalty on that basis, a backward-looking inquiry to determine "what damage has been demonstrated to have been caused by the breach or failure of the relevant provision in order to found some relief for such breach or failure". His Honour emphasised (at [137]) that the question whether the late payment fees were a penalty was to be assessed, not by reference to the damage actually caused by late payment, but at the time of entry into the contract on a forward-looking basis and by reference to whether the fee:

> "Is extravagant or exorbitant by reference to the obligee's legitimate interest in the performance of the contract assessed by the greatest loss that could conceivably be proved to have followed from a breach or failure to comply."

His Honour also observed that whether a clause was penal was to be assessed (at [147]) by reference to a "prospective assessment of compensation commensurable with the interest of the obligee protected by the bargain". His Honour's approach placed particular focus on the interest to be protected by the relevant contract, and to that extent anticipates the approach subsequently adopted by the UK Supreme Court in *Cavendish Square Holding* above.

Allsop CJ expressed the view (at [169], [173]) that Gordon J had incorrectly undertaken an *ex post* inquiry as to the loss actually suffered by ANZ and had taken too narrow a view as to the matters which could be taken into account in determining the "greatest possible loss on a forward-looking basis" by reference to "the economic interest to be protected" by ANZ. His Honour observed that the applicants' expert accounting evidence, which was directed to ANZ's actual loss rather than to a forward-looking analysis, did not support a characterisation of the late payment fee as extravagant or unconscionable. His Honour held that the several categories of ANZ's anticipated costs referable to loan provisions, regulatory capital and fixed collection costs could also properly be taken into account in determining ANZ's commercial interest to be protected by the imposition of a late payment fee.

His Honour also held that a contravention of the statutory provisions was not established in the absence of any allegation of sharp practice by ANZ, and where Mr Paciocco was aware of the relevant fees, chose to operate his credit cards in a manner which exposed him to the risk of those fees, and the relevant contracts were neither unfair nor unjust.[6]

Cavendish Square Holding

After the Full Court had delivered its decision in *Paciocco FCAFC*, the Supreme Court of

[6] For commentary as to the decision of the Full Court of the Federal Court of Australia (and the anterior decisions), see J Stumbles, "The Reach and Application of the Penalty Doctrine in Australia after Andrews v ANZ", Paper delivered at the Supreme Court of New South Wales Judge's Conference, September 2015; R McDougall "Penalties in Commercial Contracts since Andrews v ANZ", Paper delivered at CLE Seminar: Business Law, March 2016; G Westgarth and M Legg, "Bank Fees Class Action in Australia fails before Full Court" (2015) 26 *JBFLP* 111; K Barnett, "Paciocco v Australia and New Zealand Banking Group Ltd: Are late Payment Fees on Credit Cards Enforceable?" (2015) 37 *Sydney L Rev* 595.

the United Kingdom in turn addressed the relevant issues in *Cavendish Square Holding/ Parking Eye* above.[7] Those decisions involved two challenges to alleged penalties. In *Cavendish Square Holding*, the relevant clause was contained in a commercial contract and provided that, in the event of breach of a non-compete provision, the selling shareholder was not entitled to further payments and the other party could buy its remaining shares at a price which disregarded goodwill. In *Parking Eye*, the relevant clause in a parking contract imposed a substantial fee if customer overstayed the two hour free parking limit in a shopping centre. Seven judges sat in those cases and the Court's judgment is lengthy. The Court held that penalty principles under English law should not be abolished or restricted, as *Cavendish Square Holding* had contended, or extended. There are differences in their Lordships' reasoning beyond that point.

Lord Neuberger and Lord Sumption (with whom Lord Carnwath agreed) referred to *Andrews HCA* which they characterised (at [41]) as a "radical departure from the previous understanding of the law" and observed (at [42]) that they were not persuaded that the penalty principle should apply beyond the case of a breach of contract.[8] Their Lordships also observed that a clause which was a primary obligation, rather than a secondary obligation arising on breach, would generally not constitute a penalty and held that the contractual provisions in *Cavendish Square Holding* fell in that category. They observed (at [32]) that, where a clause is a secondary obligation:

> "The true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation."

That approach departed from earlier English authority, in holding that a clause could be enforceable although it was not a genuine pre-estimate of loss, if it did not impose a detriment on the party in breach of contract that is disproportionate to the legitimate interest of the innocent party. In *Parking Eye*, that approach supported a result that a substantial fee imposed for overstaying a two hour limit for free parking in a shopping centre was not a penalty, although it was also not a genuine pre-estimate of the relevant loss, where the owner of the shopping centre (and, by extension, the car park operator) had a commercial interest in promoting compliance with the time limit so as to generate customer flow for the shopping centre. There is an open question, as to which English commentators are not of a common view, as to whether the approach adopted by Lord Neuberger and Sumption was supported by a majority of the Court.

---

[7] For commentary, see M Stamp, The Penalties Rule in Corporate Contracts – Is it Offside? (2016) 37(7) *Comp Law* 219–222; D Galeza, "Getting Rid of the Penal Doctrine – The Implications of the Joint Cases Cavendish Square v L Makdessi and Parking Eye v Beavis" (2016) 27(6) *ICCLR* 175–176; W Day, "A Pyrrhic Victory for the Doctrine Against Penalties: Makdessi v Cavendish Square Holding BV" (2016) *JBL* 115 – 127; W Day, "Penalty Clauses following Makdessi: Postscript" (2016) *JBL* 251–252; J Morgan, "The Penalty Clause Doctrine: Unlovable but Untouchable" (2016) 75 *CLJ* 11–14; B Lindsay, "Penalty Clauses in the Supreme Court: A legitimately interesting decision?" (2016) 20 *Edin LR* 204–210.

[8] In *Paciocco HCA* above, French CJ described the Supreme Court's disagreement with *Andrews HCA* as "emphatic" (at [7]), while noting that the shared heritage of English and Australian Courts did not require their law to develop on similar lines, and Gageler J (at [121])ff expressed the view that the Supreme Court had misunderstood the scope of the decision in *Andrews HCA*.

The other members of the Court largely agreed that the relevant provisions were not penalties, although on somewhat different grounds. Lord Mance considered that the relevant clauses in *Cavendish Square Holding* constituted a price adjustment mechanism, consistent with the reasoning of Lords Neuberger and Sumption, but also concluded that the burden imposed by the clauses was not in any event exorbitant, extravagant or unconscionable in respect of the particular breach. Lord Hodge held that the test was whether the clause involved an “extravagant disproportion between the stipulated sum and the highest levels of damages that could possibly arise from the breach”, and held that neither clause was exorbitant or unconscionable when measured against the purchaser’s legitimate interests. Lord Clarke indicated agreement with Lords Neuberger and Sumption, but also indicated his “present inclination” was to agree with Lord Hodge and Mance in applying a test whether a clause was “exorbitant” or “unconscionable” to determine whether it was a penalty; Lord Toulson applied the same approach.

Torchlight Fund

Also subsequent to the decision in *Paciocco FCFCA*, but prior to the High Court’s decision, the High Court of New Zealand (Muir J) considered the question of penalties in *Torchlight Fund No 1 LP (in receivership) v Johnstone & Ors* [2015] NZHC 2559, although the governing law of the contract at issue in that case was the law of New South Wales in respect of the relevant contract. The case involved a substantial additional weekly amount (to use a neutral term) which was payable where a short term loan was not repaid by the date on which repayment was due. Muir J held that that amount was payable on breach, and that the amount was sufficiently disproportionate to the loss which could be suffered by the lender on late payment to constitute that fee extravagant and a penalty. I understand that an appeal from that decision will be heard in October 2016.

The Paciocco proceedings in the High Court

Two appeals were brought in the High Court in *Paciocco HCA*, the first relating to the question whether the late payment fee in respect of credit cards (which was the only fee that remained in issue) was unenforceable as a penalty at general law, and the second as to whether that fee contravened the statutory prohibitions against unconscionable conduct, unjust transactions and unfair contract terms. The Court emphasised that the late payment fee was payable in respect of a breach of contract, so the issue was whether it was a penalty in contract rather than in equity. Importantly, the majority (Nettle J dissenting) held that the losses that could be taken into account in determining whether a secondary stipulation is extravagant and unconscionable are not limited to damages that would be recoverable under the rule in *Hadley v Baxendale* (1854) 23 LJ Ex 179; (1854) 156 ER 145 if the obligee (bank) sued the obligor (cardholder) for breach of contract. The majority also held, consistent with the views taken by the Full Court of the Federal Court, that loss provision costs, regulatory capital costs and fixed collection costs were properly taken into account in determining whether the late payment fee was a penalty, and that the applicants had not established that fee was a penalty given the potential size of those costs. The Court also upheld the Full Court’s decision that the contractual provision for, and the imposition of, the late payment fee did not infringe the relevant statutory provisions.

French CJ agreed with the observations of Kiefel J as to why the late payment fees did not constitute a contractual penalty and with the observations of Keane J as to why they did not breach the statutory provisions, and also commented, as I have noted above, on the differences between the approach in *Andrews HCA* and *Cavendish Square Holding.*

Kiefel J referred to the observations of Lord Dunedin in *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* above and emphasised the requirement that a stipulated sum be "extravagant and unconscionable" before it could be characterised as a penalty and in turn identified the question (at [29]) as whether the relevant payment was "out of all proportion to the interests of the party which it is the purpose of the provision to protect". Her Honour noted that an interest may be of a business or a financial character and observed that it did not follow from *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* that a term which reflected, or attempted to reflect, "other kinds of loss or damage to a party's interests beyond those directly caused by the breach will be a penalty". Kiefel J recognised (at [58]) that ANZ had an interest in receiving timely repayment of the credit that it extended to its customers; noted the impact of late payments in respect of operational costs, loss provisions and increases in regulatory capital costs; and observed (at [68]) that those costs were real and that it could not be concluded that the late payment fee was out of all proportion to ANZ's identified interests or was a penalty. Her Honour also agreed (as had French CJ) with Keane J's observations as to the reasons why there was no breach of the statutory provisions.

Gageler J emphasised (at [122]) that *Andrews HCA* had not disturbed the existing approach to penalties at common law, but confirmed that the equitable jurisdiction in respect of relief against penalties had not been abolished, although, he added, the occasions for equitable intervention would be comparatively rare. His Honour also referred to *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* above and subsequent Australian decisions, and held (at [159], [161]–[162]) that the obligee's interest which was relevant need not be an interest for which compensation was recoverable for breach of contract. His Honour summarised the inquiry (at [164]) as whether a stipulation is "properly characterised as having no purpose other than to punish". By contrast with the reasoning in the Full Court of the Federal Court in *Andrews FCAFC*, Gageler J observed that the applicants' *ex post* analysis of costs incurred by ANZ as a result of a late payment was relevant, but his Honour also held that it was of limited utility because it had been confined to incremental operational costs and did not reflect the totality of ANZ's interest in prompt payment of the minimum amount. His Honour also held (at [171]–[172]) that loss provisioning costs and regulatory capital costs, although they could not be recovered in a claim against an individual customer, were relevant interests of ANZ in determining whether the late payment fee was a penalty and were not grossly disproportionate to the amount of that fee (at [173]–[174]) and that ANZ also had a commercial interest in avoiding or minimising fixed costs associated with its collection activities. His Honour held (at [176]) that such costs represented a commercial interest of ANZ in achieving payment of the minimum amount and it could not be concluded that the late payment fee was punitive. His Honour also held (at [191]) that the stipulation for a late payment fee was not unconscionable and the arguments as to unjust contracts failed for the same reason.

Keane J observed (at [216]) that it was difficult to infer that the purpose of the late payment fee was punitive, where the bank's legitimate interests were not confined to reimbursement of its direct costs resulting from default. His Honour pointed (at [220]) to the importance of the values of commercial certainty and freedom of contract and observed that:

> "The Courts will not lightly invalidate a contractual provision for an agreed payment on the ground that it has the character of a punishment."

His Honour also observed (at [221]) that an agreed payment should be struck down where a "gross disproportion is such as to point to a predominant punitive purpose" and that, if the provision is not "distinctly punitive", then the penalty rule did not displace the parties' ability to agree to a contractual allocation of benefits and burdens and rights and liabilities following a breach of contract. His Honour also held (at [222]) that the decision in *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd above* did not support a narrow view of the interests that could legitimately be protected by a provision for an agreed payment. His Honour held, similarly to Gageler J, that the applicants' evidence as to actual loss suffered by ANZ was not irrelevant, but also did not show the damage that might conceivably have been suffered to interests that ANZ was entitled to protect. His Honour expressly rejected (at [282]–[283]) the view that the penalty rule was limited to taking into account the damages recoverable in a claim for breach of contract. Keane J also dealt with the statutory causes of action at some length (at [286])ff) and noted that no allegations of misuse of market power, concealment, or financial pressure were made against ANZ, that Mr Paciocco had been under no obligation to use the account, and that ANZ's terms were consistent with those of other banks, and emphasised that Mr Paciocco had chosen to manage the accounts in the particular manner for his convenience, and held that claims of unconscionable conduct, unjust transactions or unfair terms had not been established.

Nettle J, dissenting, concluded that the late payment fee was penal and therefore did not address the position as to the statutory claim. His Honour held (at [321]-[323]) that the case was a simpler case of the kind contemplated by *Dunlop*, where ANZ's interest did not extend beyond the additional costs imposed by reason of a breach of the relevant contract, which would have been recoverable in a claim for breach of contract. His Honour applied substantially the same test that the majority (at [331]) namely whether the amount of the fee was "wholly disproportionate to the greatest costs which could have been conceived of at the time of entry into the contract", but differed from the majority, and from the Full Court of the Federal Court, as to the costs which should properly be taken into account in determining that question. His Honour held that the Full Court had erred in taking into account the other costs such as loss provisioning costs and regulatory capital costs, which he observed had a relationship to the breach but were too remote to be recoverable as damages for breach of contract. His Honour was also not persuaded by the methodology of ANZ's accounting expert, and agreed with the reasoning of the trial judge in that respect.

Implications

I should now highlight the broader implications of these decisions, without seeking to forecast the effect of the judgment in *Paciocco HCA* on other class actions against banks, and other utilities, which is plainly a matter for others:

- First, the position in Australian, following *Andrews HCA*, is that the equitable jurisdiction remains available in respect of clause that is collateral or accessory to a primary stipulation, contrary to the view taken by the United Kingdom Supreme Court in *Cavendish Square Holding*. That jurisdiction was invoked, but a penalty not established, in respect of fees other than the late payments fees from credit cards in *Paciocco FCA and Paciocco FCAFC*. However, Gageler J observed in *Paciocco HCA* that occasions for equitable intervention may be comparatively rare.

- Second, the approach adopted by the majority in *Paciocco HCA* focusses on the legitimate interests of the party which has the benefit of the relevant clause as determined at the time of entry into the contract. There may be a question whether that approach extends as far as the range of interests that may be taken into account under the approach of Lord Neuberger and Lord Sumption in *Cavendish Square Holding*.

- Third, the decision in *Paciocco HCA* establishes that the range of loss (or costs) taken into account in determining whether a clause is a penalty is not limited by rule in *Hadley v Baxendale* above. So far as the judgment permits a wider range of costs to be taken into account in determining, at the time of entry into a contract, whether a payment on breach or as a secondary stipulation is extravagant or unconscionable, then it will presumably be less likely that a penalty will be established. The difference may, however, be less significant in areas where the only relevant costs would have been recoverable as contractual damages, and a fee that is in fact extravagant, by reference to foreseeable costs, would still constitute a penalty at general law or in equity.

- Fourth, the decisions in *Paciocco FCAFC* and *Paciocco HCA* both indicate that breach of statutory provisions dealing with unconscionability and unfair contracts will not readily be established by criticism of the level of the price for a service, at least in an apparently competitive market, absent evidence of misuse of market power, concealment, financial pressure etc.

A subsequent decision

Since the decision in *Paciocco HCA*, the application of the penalty principle has arisen in an application to set aside a creditor's statutory demand[9] in the Supreme Court of New South Wales, in *Sydney Constructions and Developments Pty Ltd v Reynolds Private*

[9] The question in such an application is, of course, whether there is a genuine dispute as to the debt, in the sense that there is a serious question requiring further investigation as to the existence or amount of the debt.

Wealth Pty Ltd [2016] NSWSC 1104. Sydney Constructions and Developments Pty Ltd ("SCD") had entered an agreement ("MSA") with Reynolds Private Wealth Pty Ltd ("Reynolds") by which Reynolds was to seek loan funds for and introduce financiers to SCD. The MSA provided that a substantial "Entry Fee" would be payable when SCD received an offer of a loan, and the fee was also payable if SCD asked someone else to provide the loan during the "exclusive period" of the MSA. A dispute was raised as to whether the exclusivity of the agreement had been waived, which it is not necessary to address here. SCD also contended that there was a serious question as to whether the provision for payment of the "Entry Fee" on breach of the exclusivity provision was unenforceable as a penalty.

Barrett AJA held that a genuine dispute existed as to that question, since a breach of the exclusivity provision would require SCD to pay the Entry Fee whether or not it had obtained finance from an alternate source, and at the same time relieve Reynolds from any obligation to provide the relevant service. His Honour referred to *Paciocco HCA* and observed (at [50]) that, but for the relevant provision in the MSA, a breach of the exclusivity term might have supported a claim by Reynolds for damages on a loss of opportunity basis which would generally not be a claim for damages equal to the whole of the Entry Fee. On that basis, his Honour held (at [51]) that there was

> "a cogent argument (requiring further investigation) that the provision of the MSA which, upon breach of the exclusivity provision by the client, relieves the broker of its performance obligation and requires the client to pay in full the sum that would have been payable in return for due discharge of that performance obligation does not involve a genuine pre-estimate of the broker's probable or possible interest in the performance of the principal obligation and is in the nature of a punishment for non-observance of the exclusivity obligation."

Recent decisions under the Personal Property Securities Act

The question of priority over leased equipment, following the commencement of the *Personal Property Securities Act* 2009 (Cth) ("PPSA") was considered by Brereton J in *Maiden Civil (P&E) Pty Ltd; Albarran v Queensland Excavation Services Pty Ltd* (2013) 277 FLR 337; [2013] NSWSC 852. The question of vesting of leased equipment in a company, under s 267 of the PPSA, was considered in *White v Spiers Earthworks Pty Ltd* (2014) 99 ACSR 214; [2014] WASC 139; an appeal from that decision is pending. That section broadly provides for a security interest to vest in the company that granted it, if an order is made for the winding up of the company or an administrator is appointed or a deed of company arrangement executed, and the security is unperfected on the date the winding up is taken to commence under ss 513A–513C of the *Corporations Act*.

Issues as to the effect of non-registration of a security interest in respect of leased equipment under s 267 of the PSA were again considered by Hammerschlag J in *Forge Group Power Pty Ltd (in liq) (recs & mgrs apptd) v General Electric International Inc*

(2016) 305 FLR 101; [2016] NSWSC 52.[10] In that case, General Electric International Inc ("GE") leased several gas turbine generator sets to Forge Group Power, which was subsequently placed in administration and then under liquidation. GE had not registered its interest in that equipment under the PPSA. Forge contended that, because GE's security interest was not perfected when the administrator was appointed, that interest vested in Forge on the appointment of the administrator under s 267 of the PPSA. GE unsuccessfully contended that the relevant arrangement was not a "PPS lease" on the basis that GE was not regularly engaged in the business of leasing goods. Hammerschlag J held that that concept was not limited to leasing in Australia, and whether GE fell within that exception was to be determined at the time of entry into the lease; and that the exception was not satisfied where, at that time, GE regularly engaged in the business of leasing goods. GE was also unsuccessful in establishing its second contention, which was possibly counter-intuitive when put by a lessor, that the generators were fixtures and outside the scope of the PPSA. The decision is another illustration of the significant risk of vesting of secured property in an administration, where a security interest is not registered under the PPSA.

Section 588FL of the *Corporations Act* in turn provides that certain interests covered by the PPSA that are not registered within a specified time vest in the company that is being wound up in administration; vesting was established on that basis in *Carrafa (as liquidators of Relux Commercial Pty Ltd) (in liq) v Doka Formwork Pty Ltd* (2014) 104 ACSR 163; [2014] VSC 570.

Effect of deeds of company arrangement on secured creditors

Complex questions as to whether a secured creditor's debt survives a deed of company arrangement that purports to extinguish it, under s 444D(2) of the *Corporations Act*, were considered by the Supreme Court of Western Australia in *Australian Gypsum Industries Pty Ltd v Dalesun Holdings Pty Ltd* (2015) 106 ACSR 79; [2015] WASCA 95 and in *Re Bluenergy Group Ltd (subject to a deed of company arrangement) (admin apptd)* (2015) 107 ACSR 373; [2015] NSWSC 977.

These issues turn upon s 444D of the *Corporations Act* which relevantly provides that:

> "(1) A deed of company arrangement binds all creditors of the company, so far as concerns claims arising on or before the day specified in the deed under paragraph 444A(4)(i).
>
> (2) Subsection (1) does not prevent a secured creditor from realising or otherwise dealing with the security interest, except so far as:
>
> (a) the deed so provides in relation to a secured creditor who voted in favour of the resolution of creditors because of which the company executed the deed; or

[10] For commentary, see A Staples and M Hilton, "Regularly Lease Goods? Remember to Register Regularly" (2016) *ABFLB* 57; C Wappett, "Equipment Leasing and the PPSA – Another painful lesson for Lessors" (2016) *Insolvency Law Bulletin* 32.

(b) the Court orders under subsection 444F(2).”

In *Hamilton v National Australia Bank Limited* (1996) 66 FCR 12, Lehane J held that s 444D(2) preserved a secured creditor’s proprietary and contractual rights and powers under a security in relation to property affected by that security. In *Australian Gypsum Industries Pty Ltd v Dalesun Holdings Pty Ltd* above, the Court of Appeal of the Supreme Court of Western Australia addressed the question whether s 444D of the *Corporations Act* preserves a security in relation to a claim that arises after a release becomes effective under a deed of company arrangement. In that case, BGC Group had supplied goods and services to Newglen Nominees Pty Ltd (“Newglen”), supported by a guarantee provided by Dalesun Holdings Pty Ltd (“Dalesun”)which was secured by an equitable charge over land held or to be held by Dalesun. Dalesun was subsequently placed in administration and executed a deed of company arrangement that extinguished claims of creditors, other than several identified secured creditors, and did not preserve BGC Group’s claim. BGC Group had not been given notice of the second meeting of creditors in respect of Dalesun’s administration and had not voted in favour of the resolution of creditors at that meeting for the purposes of s 444D(2). BGC Group subsequently supplied goods to Newglen which itself then went into administration. BGC Group claimed under the guarantee given by Dalesun and sought a declaration that it held an equitable charge over land held by Dalesun. Its entitlement to such a charge depended on whether its claim under the guarantee given by Dalesun survived Dalesun’s deed of company arrangement. The majority in the Court of Appeal there referred to the approach in bankruptcy law and to the purposes of Pt 5.3A of the *Corporations Act* and held that the deed of company arrangement entered by Dalesun was capable of extinguishing contingent debts or claims secured by the guarantee which arose at a later date. Although that decision has been criticised by one commentator as inconsistent with case law dealing with when the extinction of a principal debt extinguishes a guarantee, the question in issue in that case was not whether the guarantee was released, but what obligations remained subject to it.

In *Re Bluenergy Group Ltd* above, a second-ranking secured creditor, Keybridge Capital Limited (“Keybridge”), held security over all present and future acquired property of Bluenergy Group Ltd (subject to Deed of Company Arrangement) (Administrator Appointed) (“Bluenergy”), and abstained from voting on a resolution to approve a deed of company arrangement. After the execution of that deed of company arrangement, which released the debts of other creditors, Keybridge relied on its status as a secured creditor to appoint a second administrator. The Court followed the decision in *Australian Gypsum Industries Pty Ltd v Dalesun Holdings Pty Ltd* above, although a submission was made by Counsel that that decision was plainly wrong. The Court also held that s 444D(2) of the *Corporations Act* preserved Keybridge’s security interest in the property to which it attached at the date of the release under the deed of company arrangement, and that it was entitled to appoint a second administrator since it remained a secured creditor over substantially the whole of the company’s property. However, the Court held that that section did not have the result that Keybridge remained a creditor for any other purpose, and distinguished (at [63]) between the personal rights of a creditor in debt, which can potentially be extinguished by a release of the debt under a deed of company arrangement in accordance with s 444D(1), and the proprietary interest of a secured creditor preserved by s 444D(2) in respect of the debt and the secured assets available to the secured creditor when that release took effect. The Court observed (at [66]) that:

> "… s 444D(2) of the *Corporations Act* can be given effect, in accordance with its terms, by preserving the secured creditor's property right in its security interest, in respect of the property to which it was capable of attaching at the date a release under a deed of company arrangement would take effect, without recognising a preservation of rights over after-acquired property extending indefinitely into a company's future."[11]

The Court ordered that the second administration be terminated under s 447A of the *Corporations Act*, where it found that its continuance would be inconsistent with the purposes of Pt 5.3A of the *Corporations Act*, and that there was no utility in that administration where Keybridge was not a creditor in it and the administrators in the first administration, who may be the only creditor in it, opposed its continuance.

Extension of time for proceedings brought by a liquidator under s 588FF of the Corporations Act

Section 588FF of the *Corporations Act* specifies the orders that a court may make if a transaction is voidable under s 588FE of the *Corporations Act*, as an insolvent transaction including an unfair preference (within the scope of s 588FA), an uncommercial transaction of the company (within the scope of s 588FB), an unfair loan to the company (within the scope of s 588FD) or an unreasonable director-related transaction (within the meaning of s 588FDA). An application under this section may be made during the period beginning on the relation-back day (as defined in s 9) and ending on the later of 3 years after the relation-back day or 12 months after the first appointment of a liquidator in relation to the winding up of the company or within such longer period as the court orders on an application by the liquidator brought within that period.[12]

The power to make "shelf orders" which extend the time for a liquidator to bring proceedings in relation to voidable transactions that are not identified at the relevant time, has been recognised at least since *BP Australia Ltd v Brown* (2003) 58 NSWLR 322; (2003) 46 ACSR 677; [2003] NSWCA 216 and was reconfirmed on appeal in *Fortress Credit Corporation (Australia) II Pty Ltd v Fletcher* (2015) 254 CLR 489; (2015) 89 ALJR 425; [2015] HCA 10. The interaction between s 588FF and the Court's procedural rules, including for extensions of time, was also considered by the High Court of Australia in *Grant Samuel Corporate Finance Pty Ltd v Fletcher* (2015) 254 CLR 477; (2015) 89 ALJR 401; [2015] HCA 8. The High Court emphasised that the commencement of preference proceedings within the time limit under s 588FF(3), as extended under s 588FF(3)(b) was a precondition to the Court's jurisdiction under s 588FF; and held that s 588FF "otherwise provided" for the purposes of s 79 of the *Judiciary Act* 1903 (Cth), so that an extension of time under that section could not be supplemented or varied by procedural rules of the Court in which the application has been brought.

---

[11] That reading of s 444D(2) of the *Corporations Act* is broadly consistent with the approach adopted in s 153(3) of the *Bankruptcy Act* 1966 (Cth) which deems a secured debt to continue, despite a release or discharge of the bankrupt, to facilitate a creditor's dealings with the secured property.

[12] *Corporations Act* s 588FF(3)(a)-(b).

In a third decision, in *Fletcher v Anderson* (2014) 293 FLR 269; (2014) 103 ACSR 236; [2014] NSWCA 450, the Court of Appeal considered the position in respect of preference claims against the Commissioner of Taxation under s 588FA of the *Corporations Act* and consequential claims to indemnity under s 588FGA of the *Corporations Act*. The Court of Appeal observed that s 588FGA(2) of the *Corporations Act* creates a statutory liability on the part of the director, in respect of the claim against the Commissioner of Taxation, whether or not the Commissioner ultimately brings proceedings to enforce that statutory liability, and also held that directors were immediately affected by the extension order made under s 588FF of the *Corporations Act* and should have been given notice of the application and an opportunity to be heard. However, the result was not that the extension order should necessarily be set aside, but instead that they should be allowed a further opportunity to be heard as to the question whether that order should have been made.

In *Re Cardinal Group Pty Ltd (in liq)* (2015) 110 ACSR 175; [2015] NSWSC 1761, I granted leave to liquidators to amend a statement of claim to extend their preference claim, where the particular dealings which were the subject of that claim were outside the three year period specified in s 588FF(3) of the Act. I followed the earlier decision of the Full Court of the Federal Court of Australia in *Rodgers v Federal Commissioner of Taxation* (1998) 88 FCR 61; 29 ACSR 270, where the Full Court had held that amendment to an existing proceeding, commenced within time, could add separate transactions based on substantially the same facts. I distinguished the decision in *Fortress Credit Corporation* above on the basis that it concerned the commencement of new proceedings and also noted that, in the particular case, the claim could have been pleaded as a single transaction and the particular dealings that were introduced in the claim could have been added by way of further particulars of that transaction. An appeal from that decision has now been heard by a five-member Court of Appeal and judgment is reserved.

Insolvency Law Reform Act

I should also mention the passage of the *Insolvency Law Reform Act* 2016 (Cth). The possibility of amendments to insolvency law was raised by a Discussion Paper issued by the Senate Economic References Committee, *The Regulation, Registration and Remuneration of Insolvency Practitioners in Australia: The case for a new framework* (2010). The amendments would amend both the *Bankruptcy Act* 1966 (Cth) and the *Corporations Act* to introduce common rules in relation to the registration, regulation, discipline and the registration of corporate and personal insolvency practitioners. The Explanatory Memorandum to the Exposure Draft identified the purpose of the proposed amendments as including removing unnecessary costs and increasing efficiency in insolvency administrations, aligning and modernising the registration and disciplinary frameworks that apply to registered liquidators and registered trustees in bankruptcy and rules relating to personal bankruptcies and corporate external administrations; promoting market competition on price and quality and “improv[ing] overall confidence in the professionalism and competence of insolvency practitioners".[13]

The *Insolvency Law Reform Act* will repeal a number of sections that are commonly relied on in applications to the Courts in insolvency matters, including s 479 (exercise and control of a court-appointed liquidator's powers), ss 502–505 (appointment and removal of a liquidator in a voluntary winding up, review of a liquidator's remuneration), s 511 (applications to the Court to have questions determined or powers exercised in a voluntary winding up), s 536 (supervision of liquidators) and ss 600A–600E (Court's powers in respect of resolutions passed at creditors' meetings). There are complex transitional provisions. Some broadly corresponding powers will be introduced in the Insolvency Practice Schedule (Corporations) contained in proposed Schedule 2 of the *Corporations Act*. It is expected that Parts 1 and 2 of the Insolvency Practice Schedule (Corporations) (dealing with registration and discipline of liquidators) will commence on 1 March 2017 and Part 3 (dealing with general rules for the conduct of external administrations) will commence on 1 September 2017.

Division 45 of the Insolvency Practice Schedule (Corporations) allows the Court specified powers in relation to registered liquidators, including on its own initiative in Court proceedings or on application by the liquidator or ASIC. Division 60 Subdiv B permits an external administrator[14] to claim remuneration specified in a "remuneration determination" made by, inter alia, the Court. The Court can also review an external administrator's remuneration, including ordering repayment of remuneration.

Division 70 Subdiv G allows the Court (and also ASIC) a new power to direct an insolvency practitioner to provide information, including information requested by creditors. The Court retains the power to inquire into an external administration under Div 90 Subdivs B and C. In particular, s 90-15 allows the Court to make such orders as it thinks fit in relation to the external administration of a company. The Court can exercise that power on its own initiative, during proceedings before the Court; or on application by specified persons under s 90-20. Section 90-15(3) gives examples of such orders[15] and s 90-15(4) specifies matters which the Court may take into account when making such orders. Div 100, s 100-5 will allow an external administrator to assign any right to sue conferred on him or her by the *Corporations Act*, but court approval for that assignment is required after any action brought by the external administrator has begun.

[13] Explanatory Memorandum to the Exposure Draft of the Insolvency Law Reform Bill 2014, p 3.
[14] Div 5, cl 5-20 of the Insolvency Practice Schedule (Corporations) provides that an external administrator is an administrator of a company, the administrator of a deed of company arrangement in respect of the company or the liquidator or provisional liquidator of the company.
[15] Those examples are an order determining any question arising in the external administration of the company; an order that a person cease to be the external administrator of the company; an order that another registered liquidator be appointed as the external administrator of the company; an order in relation to the costs of an action (including court action) taken by the external administrator of the company or another person in relation to the external administration of the company; an order in relation to any loss that the company has sustained because of a breach of duty by the external administrator; and an order in relation to remuneration, including an order requiring a person to repay to a company, or the creditors of a company, remuneration paid to the person as external administrator of the company.

Safe harbours from insolvent trading

In its Proposals Paper, *Improving Bankruptcy and Insolvency Laws* (April 2016), the Commonwealth Government raises the possibility of introducing two forms of safe harbour to limit the risk of personal liability for directors for insolvent trading, where a director is involved in restructuring efforts. The Proposals Paper identifies the rationale for the reform as that it would strengthen Australia's "start-up culture" by moving from a regime that penalises directors and stigmatises failure, so as to encourage entrepreneurship and assist start-ups in attracting experienced and talented board members. I note, in passing, that that rationale may seem somewhat distant from the bulk of insolvency matters dealt with by insolvency practitioners and the courts, which have little to do with start-ups, innovation or the new economy. It is likely that the proposed reforms would impact on a much larger number of cases dealt with by insolvency practitioners and courts which do not fall within their stated rationale.

The first proposed form of safe harbor ("Safe Harbour Model A") would provide a defence where a director has an expectation, based on advice received from an appropriately experienced, qualified and informed restructuring adviser[16], that the company can be returned to solvency within a reasonable period of time and the director is taking reasonable steps to do so. The defence would only apply in respect of liability for insolvent trading, and not for all potential breaches of the *Corporations Act*. The risk of misuse of this defence would be reduced by the proposed requirement that the restructuring adviser be provided with appropriate books and records within a reasonable time from his or her appointment and then remains of the opinion that the company can avoid insolvent liquidation and is likely to be returned to solvency within a reasonable period of time. Those companies where the risk of abuse of this provision would be at its greatest may well be unable to comply with that requirement. The defence would also not be available were the company had failed to lodge multiple business activity statements or there was a significant failure to pay employee claims, PAYG tax or employer superannuation requirements, and would also not prevent civil claims against directors relating to outstanding employee entitlements that accrued during the safe harbour period. The Government does not propose to relax continuous disclosure requirements in respect of entry into such an arrangement. There would be practical questions whether a listed company's reliance on the safe harbour would generally be disclosable and whether unsecured creditors will be reluctant to trade with a listed public company after such a disclosure.

An alternative form of safe harbour ("Safe Harbour Model B") would apply to particular debts incurred as part of reasonable steps to maintain or return a company to solvency within a reasonable period of time, where a person held an honest and reasonable belief that incurring the debt was in the company's best interests and creditors as a whole and incurring the debt did not materially increase the risk of serious loss to creditors. We should recognise that this approach appears to contemplate that the safe harbour is

[16] The restructuring adviser would be excluded from the definition of director so as not to be at risk of being held to be a shadow or de facto director, and would be required to report any misconduct that he or she identified to ASIC. The restructuring adviser would also be protected against third party claims, provided his or her opinion was honestly and reasonably held.

available where incurring the debt will expose a particular creditor to an increased risk of serious loss, provided that it does not increase the risk of serious loss to creditors generally. Where a company is large and its debts are substantial, a debt incurred to a particular creditor may be of real commercial significance to that creditor although it does not materially affect the position of the company's creditors generally. This alternative does not necessarily involve the retainer of an insolvency practitioner to provide restructuring advice, although expert advice would no doubt assist directors in establishing the existence of an honest and reasonable belief as to the relevant matters.

This proposal appears to have been generally welcomed by the insolvency profession. There are plainly arguments that are capable of being put each way. On the one hand, the Australian insolvent trading regime is significantly more onerous than comparable regimes in other developed economies,[17] and there is a strong case that the insolvent trading regime operates as a significant practical disincentive to informal workout arrangements, and encourages the appointment of an administrator at an earlier rather than a later point. The contrary view is that individual creditors, or creditors generally, may, possibly unknowingly, bear the risk that a restructuring proposal fails and they are left without recourse for debts incurred in the course of it.

[17] J Harris, "Director Liability for Insolvent Trading: Is the Cure Worse than the Disease" (2009) 23 *AJCL* 266.