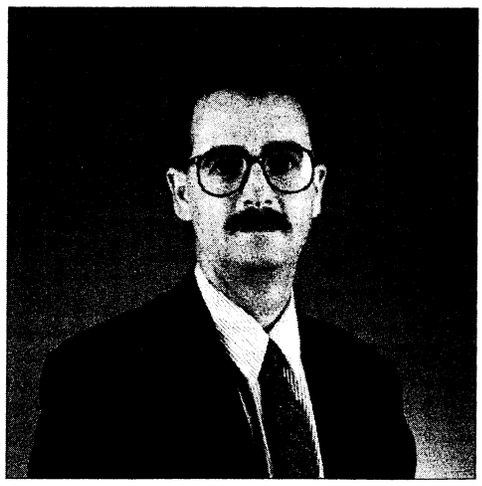
"Suspicion or mere idle wondering"

Should the timing of the availability of accounting information be relevant in assessing whether directors have reasonable grounds to suspect that a company is unable to pay its debts ? As stated by Kitto J in *Queensland Bacon (1)* , "a suspicion that something exists is more than a mere idle wondering....". This was also one of the issues considered in the Full Court's decision in *Kong v Pilkington (2)*.



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Objective facts

Often the term "technically" insolvent is used to explain a company's overall deficiency of assets position, yet such companies continue to trade, for example, based upon the continuing support of shareholders and financiers. Similarly, it is often argued that a net deficiency of liquid assets (eg trade debtors less than trade creditors) also proves insolvency.

However, in our experience neither of these views alone is sufficient to prove or conclude that a company is insolvent for the purposes of s.588G of the Corporations Law. That section uses a "reasonable grounds for suspecting" test for assessing the duties of directors in relation to insolvency.

On numerous occasions the Courts have considered the details required to assess the financial position of a company (eg *Metal Manufacturers Limited (3)*, *Statewide Tobacco (4)*). In our opinion, the Courts have always considered the objective facts such as:-

·Recent years' balance sheets and detailed statements of profit and loss, together with any periodic financial statements;

·Pattern of trading results, seasonal and historical sales and profit patterns;

·Net tangible asset position, after consideration of valuations of assets;

·"Working capital" and "Net liquid assets" positions;

·Bank balances, past and current overdraft limits, as compared to the level of overdraft, post dating/late payment of cheques, and dishonoured cheques;

·Creditors terms of trade, set off arrangements, deferred terms;

·Recoverable values of assets and related party loans.

·Ability to raise money or to pledge assets.

Our experience has shown that there is additional "ammunition" to be found by a thorough examination of company records through the process of discovery. It is also our experience that not all lawyers appreciate what that "ammunition" may be, and a vital clue to proving insolvency or otherwise may be overlooked. Examination of items such as the following may yield some benefits:-

·Correspondence with bankers/financiers;
·Listings and aging of debtors and creditors;
·Correspondence with creditors;
·Minutes of management and directors meetings;
·Bank finance applications, including supporting financial information prepared at that time.

Expert accounting advice can assist to reconstruct records where a vital piece of evidence is missing, or graphically demonstrate a deteriorating financial position.

Without considering these additio matters, only part of the "jigsaw" n be completed, and an erroneous c clusion may be reached.

Not if, but when

It would appear, *prima facie*, that t analysis of whether or not a compan insolvent is perhaps not complex. T difficulty lies, rather, in establishi grounds for insolvency based on a co sideration of all of the circumstanc and applying "commercial reality the facts" (see *Pegulan Floor Cove ings (5)*.

For example, in *Kong v Pilkington*, th defendant directors appealed that was appropriate to take into accou the fact that creditors were not pressir for payment of current debts. The Fu Court rejected that argument, statin that whether or not a debt was due, wa to be determined by reference to th legal position between the compan and the creditor. Any reluctance b creditors to enforce those legal right was irrelevant (6).

The directors also appealed on th grounds that it was appropriate to tak into account the fact that the compan had an excess of current assets ove current liabilities. The Full Court looke beyond that simplistic view of workin capital and considered the nature of the assets, finding that in the circumstances the appropriate consideration was to what extent trade debtors exceeded trade creditors, ie liquid assets. This view was taken on the basis that inventories were, to some extent, illiquid, and would take time to be realised.

Finally, the Full Court accepted the argument of the directors that, based on the facts of that case, it would be impracticable to expect the directors to form a view that the company was insolvent immediately upon receiving the interim financial statements, even though it showed a loss, as compared to previous years' profits. In the circumstances,

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Toyota Launches New Echo Mini-car

Bridge Autos Toyota offers Law Society members special discount deals. It now has in stock an all-new European-designed mini-car with advanced package efficiency and class-leading engine technology.

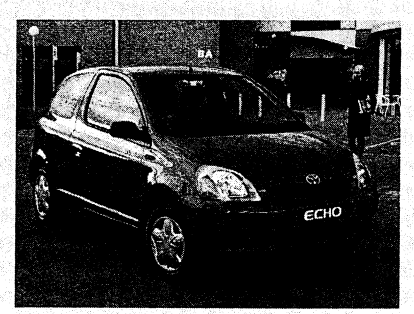
Toyota Echo is the first Toyota styled in Europe. It goes on sale in Australia on October 8, from $14,990.

Echo offers outstanding space, safety, fuel and environmental efficiency in a challenging styling package. It can accommodate four 190cm-tall adults. Australian buyers have the choice of three model variants - 3-Door and 5-Door Hatch, with a 1.3 litre engine, and a four-door sedan with a 1.5 litre engine.

Both Echo twin cam multi-valve engines have intelligent variable valve timing - a first in class and a first in Australia for a Toyota-badged vehicle. VVT-I improves torque, power and fuel economy, and reduces emissions. The 1.5 litre engine is the first mini-car engine to break the 100hp barrier. It delivers 80kW (107hp) at 6000rpm and 142Nm of torque at 4200rpm.

These engines can be matched to the five-speed manual or state-of-the-art electronically controlled four-speed automatic transmissions. Echo Hatch was designed to a "short but tall" concept, for increased interior space and better aerodynamics. At 3615mm overall length it is the shortest vehicle in the Toyota range.

Echo Hatch has a drag co-efficient of 0.30 and sedan has a coefficient of 0.29. Toyota designed Echo under its GOA (Global Outstanding Assessment) program to meet the world's toughest safety standards, including a 40 percent offset deformable barrier test at an impact speed of 64km/h - well in excess of the world test standard of 56km/h. Passive safety features include driver's airbag SRS with force-limiting seatbelt pretensioner, whiplash injury lessening (WIL) front seats, head impact protection for the pillars and roof rails and a four-way collapsible steering column.



Echo has a refined interior package which includes digital centre-mounted instruments, and tri-tone interior colours with Jacquard cloth seat trim. Echo's hip point is 580mm above the ground, for greater ease of entry and exit, and a relaxed driving position. The rear seat in Hatchback is a 60/40 split fold design which tumbles forward to create additional luggage space. Toyota Echo has more than a dozen cabin storage locations. There are various option packs, including Safety Pack, for all models.

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the Full Court allowed a period of 3 weeks to check the figures, assess the company's position, and seek expert advice.

We doubt that the three week period stated in that case is of much comfort for directors in most insolvency situations. We suggest that, in practice, the change from "mere idle wondering" to "reasonable grounds for suspecting" will not take place on receipt of a particular set of financial statements. Usually, by then, the "commercial reality" will have become all too apparent.

1. Queensland Bacon v Rees (1966) 115CLR 266.
2. Kong v Pilkington (Australia) Ltd (1997) ACLC 1561.
3. Metal Manufacturers Limited v Lewis (1988) 13 NSWLR 315.
4. Statewide Tobacco Services Ltd v Morley (1990) 8ACLC 827.
5. Pegulan Floor Coverings v Carter (1997) 15 ACLC 1293.
6. Standard Chartered Bank of Aust Ltd v Antico (1995) 13ACLC 1381.

Peter Holmes is also Chairman of the Forensic Accounting Special Interest Group of the Institute of Chartered Accountants in Australia, SA Branch.

Advocacy – Observing the Customs

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something to say and sit down to give him or her the opportunity to address the court. (4) If the conduct persists invite the court to intervene to ensure that you are able to present your case free from interruption.

You will find that if misconduct of this kind by your opponent is distracting you it will also be distracting the Bench and the jury. The Bench will not need much persuasion before it interferes.

Submissions

It is important to remember that you appear as the representative of your client and you are there to put submissions on behalf of your client. The court is not concerned with your personal views and, indeed, should not be made aware of those views. The case is not about you. It follows that when you address the court you should not be using expressions such as "I think" or "I believe". Your role is to make submissions on behalf of your client and you do this by using expressions such as "I submit" or "I contend" or "Our case is".

The Bar Table

Often you will appear before a court when a series of matters is being dealt with. This regularly occurs in Magistrates' Courts and also in the Supreme Court when interlocutory matters are being dealt with or arraignments conducted. When you are at the bar table and come to the completion of your matter you should not leave the bar table unless other counsel is taking your place. If yours is the last matter in the list or if other counsel are not assuming positions at the bar table you should remain in place. If it is necessary for you to leave then you should seek the permission of the court to do so. In the absence of permission it is a discourtesy to the Bench to leave the court facing an empty bar table.

This is a grab bag of random and incomplete observations regarding this topic. You should refer to any of the many texts on advocacy to find out more regarding matters of etiquette and appropriate conduct in court.