REMEDIES OF THE SECURED CREDITOR*

The whole body of English law could be contained in comparatively few rules had everyone sufficient money to meet the debts and legal obligations incurred by him. The complexity of the law is due either to plaintiffs searching, like plants for sunlight, for defendants with sufficient means to satisfy their causes of action, or creditors seeking priority for themselves when the available funds of the debtor are not enough to discharge all the claims thereon.¹

After experience of some of the practical problems brought by clients and considering the complexity of some of the problems in decided cases which other people's clients have been rash or rich enough to litigate I can only concur with the author. Consequently to do justice to this subject I would require the wisdom of Solomon and the reader would require the patience of Job. My paper is accordingly confined to those areas which seem to me likely to arise most frequently in practice.

REMEDIES OF THE SECURED CREDITOR

The most complex problems arise where the parties to a mortgage have not provided for the contingency which has occurred, or where such provision as there is, is ambiguous. Consequently it may fairly be said that many of the problems encountered by secured creditors are of their own making. The first requirement of the secured lender is one which it is hoped should not present any real problem and that is to find a competent lawyer and draftsman.

Today secured creditors do not as a matter of practice avail themselves of many of the remedies which are in fact available. These remedies have been described by Waldock² as falling into two groups—the final remedies of foreclosure, sale, and the personal action on the covenant, and the remedies of entry into possession and the appointment of a receiver which are not usually final remedies. Only one final remedy—that of sale, and only one of the less final remedies

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* A paper read at the Annual Summer School at the Law School of the University of Western Australia, February 1972.
² LAW OF MORTGAGES, 260.
—the appointment of a receiver, are commonly used, and the reasons for the abandonment of the other remedies should be shortly considered.

A mortgagee has historically been entitled to pursue all his remedies concurrently. He might simultaneously take proceedings for foreclosure and sue on the personal covenant. Alternatively he might pursue his remedies successively. A mortgagee was therefore largely outside the general rule that separate proceedings must not be brought for different forms of relief claimed in respect of the same transaction. However legislative restrictions on these rights have been introduced which make some of these remedies less attractive, as can be seen in the case of foreclosure.

CONSOLIDATION AND MARSHALLING OF SECURITIES

Before proceeding to consider problems associated with remedies two procedures available to mortgagees should be noted. Under the doctrine of consolidation an astute mortgagee holding two mortgages from the same mortgagor securing different amounts could refuse to allow a defaulting mortgagor to redeem one mortgage unless he redeemed the other. This doctrine although still applicable in some of the Australian states has now been abolished in Western Australia by section 56 of the Property Law Act in respect of mortgages made after the coming into operation of the Act.

However the doctrine of the marshalling of securities has so far survived legislative interference. Under this doctrine where a first mortgagee holds securities over two properties A and B and a second mortgagee holds security only over property A, then the second mortgagee has the right to require the first mortgagee to exercise his powers so as primarily to satisfy himself from the property over which he is the sole mortgagee (that is, property B). If the first mortgagee sells both properties, he must hold the aggregate proceeds on trust to pay himself first and then the second mortgagee, the mortgagor being entitled to none of the moneys until the second mortgagee has been paid. If the first mortgagee has sold property A before the intervention of the second mortgagee, then equity will protect the position of the second mortgagee by subrogating him to the rights of the first mortgagee against property B to the extent that property A would have satisfied his claim but for its sale by the first mortgagee. Of course, in all these circumstances, the second mortgagee does not gain a greater security than he otherwise would possess; he obtains nothing from either property unless the first mortgagee can be paid out in full.
Marshalling thus operates to the detriment of the mortgagor but not to that of the first mortgagee. As in practice the practitioner is usually struck with gloom when considering the position of an unpaid second mortgagee, consideration should always be given to this principle to see whether it can be used to assist what seems an otherwise hopeless case.8

**FINAL REMEDIES**

(a) **Foreclosure**

Foreclosure is an equitable right whereby the mortgagee can apply to a court for the extinction of the mortgagor's equity of redemption once the mortgagor is in default. The action has always been cumbersome in that all parties interested must be joined and accounts must be taken between such interested parties. The remedy would probably be sought where the mortgagee was distrustful of the results of an enforced sale or perhaps where the mortgagor could not be found. In any such court application the the mortgagor is given a last chance to redeem and the court will in the first instance make an order nisi giving the mortgagor a chance to pay out the sums owing in accordance with the accounts settled and requiring the mortgagee to reconvey the mortgaged property if the mortgagor does so.

The order nisi is usually for a period of six months which is Equity's last concession to the mortgagor. If payment is not made the order absolute extinguishes the equity of redemption. Foreclosure applies equally to realty and personalty but is appropriate in the case of personalty only to an assignment type mortgage and not a pledge.

Section 53 of the Property Law Act 1969 of Western Australia now indicates what a final remedy such proceedings are. Section 53(1) provides that the property taken by the decree absolute shall be in full satisfaction of the mortgage debt, and the mortgagee's right or equity to bring any action or take any other proceedings for the recovery of the mortgage money from the debtor, a surety, or any other person, is extinguished. Under sub-section (3) although a mortgagee may enforce a foreclosure on any collateral mortgage, he may not sue the mortgagor on the personal covenant in such collateral mortgage. Under section 55 of the Act it is provided that in an action for foreclosure the court may, on the request of the mortgagee or of

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3 The general principles involved and variations upon these factual situations are considered in (1965) *5 Sydney L. Rev.* 120, 120-123, 131-132.
any person interested in the mortgage money or in the right of redemption, notwithstanding the dissent of any person, if it thinks fit, direct a sale of the mortgaged property.

Consequently foreclosure is unlikely to be an attractive proposition. Its cumbersome features remain and if an order is made the mortgagee's other remedies are extinguished. In practice if an action is brought one might expect a court to favour any application for an order of sale under section 55. I do not know what the incidence of foreclosure actions in Western Australia is, but I am unaware of any action which has been brought in New South Wales in recent years. Consequently one may hope that the complex problems of redeeming up and foreclosing down may become more a matter of academic study than practical worry.

(b) Action on the Personal Covenant

An action on the personal covenant is probably the last resort of a mortgagee. There is little point in bringing such an action before the mortgagee's power of sale is exercised unless the mortgagee is satisfied that the mortgagor is a person or company of substantial means. If the action is successful in most cases this will in any event lead to a forced sale of the mortgaged property. It is for this reason obviously preferable for a mortgagee to sell first and then fall back on an action on the personal covenant for any deficiency. Actions on the personal covenant have had their own problems as legislatures have sought to restrict their scope by the introduction of moratorium legislation. Such legislation has, however, at the present time largely disappeared and so far as I am aware is not a problem in Western Australia.

It might be noted also that in Western Australia there is no equivalent of section 102 of the Conveyancing Act of New South Wales which was based on the New York Civil Code. This provides that on a Judgment of any Court for a debt secured by mortgage of any property the equity of redemption of the mortgagor shall not be taken in execution under the Judgment.

(c) Power of Sale

Generally speaking a mortgagee’s power of sale will flow both from statute and from the mortgage deed. Section 57 of the Property Law Act confers such a power and provides that it may be varied or extended by the mortgage deed. Any variations and extensions shall operate as if such variations and extensions were contained in the Act.
Under a common law mortgage, although the legal estate vests in the mortgagee, the power of sale is not a common law power. It is an equitable power which is inserted to enable the mortgagee to convey a title which is not only good at common law but good in equity to defeat the equitable rights of the mortgagor. Thus a mortgagee exercising a power of sale is selling not only his legal estate but also the equity of redemption of the mortgagor. This is recognised by section 60 of the Property Law Act which expressly states that a power of sale exercised under Part VI carries with it the interest of the original mortgagor.

Because of the equitable nature of the power of sale it is not surprising that equitable principles should have been formulated to regulate its exercise. It has sometimes been assumed that the fetters imposed by equity are not severe. However the most recent case on the subject, Cuckm饿re Brick Co. Ltd. v. Mutual Finance Ltd., suggests that they are substantially more onerous for the mortgagee than has been previously thought. It has always been well settled that a mortgagee is not a trustee of the power of sale for a mortgagor. Given this, mortgagees have tended to rely on the decision of the House of Lords in Kennedy v. De Trafford. In this case the House of Lords stated that the only obligation encumbent on a mortgagee selling under a power of sale was to act in good faith. Lord Herschell cited with approval the remarks of Lindley L.J. in the Court below:

It is not right or proper or legal for him [the mortgagee] either fraudulently or wilfully or recklessly to sacrifice the property of the mortgagor.

From this some have assumed that so long as a mortgagee acted in good faith, negligence short of gross carelessness was not material.

In the Cuckm饿re Brick Co. Ltd. case however, the Court of Appeal pointed out—
(a) That the House of Lords did not reserve in the case of Kennedy v. De Trafford;
(b) that Lord Herschell said the appeal was as hopeless as had ever been presented to the House; and
(c) that the then recently decided case of Tomlin v. Luce had not been referred to.

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7 Id. at 185.
8 (1890) 43 Ch. D. 191.
In the *Cuckmere Brick Co.* case the mortgagee exercising the power of sale was aware that the land sold had been approved both for flat and house development. He employed an experienced agent to auction the property for him. The agent did not believe that flat development was desirable or would prove profitable, and though the property was widely advertised throughout England the advertisements referred only to the approval for house development and the possibility of using the site for flat development was not mentioned. At auction the property realised £44,000 and the judge at first instance accepted evidence from other agents called by the mortgagor to the effect that it was worth £65,000 as a flat site.

Salmon L.J. stated the basic law thus:

It is well settled that a mortgagee is not a trustee of the power of sale for the mortgagor. Once the power has accrued, the mortgagee is entitled to exercise it for his own purposes whenever he chooses to do so. It matters not that the moment may be unpropitious and that by waiting a higher price could be obtained. He has the right to realise his security by turning it into money when he likes. Nor, in my view, is there anything to prevent a mortgagee from accepting the best bid he can get at an auction, even though the auction is badly attended and the bidding exceptionally low. Providing none of those adverse factors is due to any fault of the mortgagee, he can do as he likes. If the mortgagee's interests, as he sees them, conflict with those of the mortgagor, the mortgagee can give preference to his own interests, which of course he could not do were he a trustee of the power of sale for the mortgagor.9

Counsel for the mortgagee contended that the mortgagee's sole obligation to the mortgagor in relation to the sale was to act in good faith and that beyond this the mortgagee owed no duty of care. The plaintiff contended that in addition to the duty to act in good faith the mortgagee was under a duty to take reasonable care to obtain whatever was the true market value of the mortgaged property at the time of sale. The Court accepted the proposition that the mortgagee owes both duties.

Salmon L.J. analysed the position in *Tomlin v. Luce* and concluded:

It would seem, therefore, that many years before the modern development of the law of negligence, the courts of equity had laid down a doctrine in relation to mortgages which is entirely consonant with the general principles later evolved by the common law.10

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10 Id. at 644.
These propositions are an interesting example of what we in New South Wales, where we have retained (or will retain until June 1972) law and equity flowing in their separate streams, would regard perhaps as pollution of equitable principle caused by the so called "fusion" of law and equity elsewhere. The power of sale is, as I have said with the support of Sir Frederick Jordan, an equitable power, but it is here being explained in terms of "duty of care" drawn from the tort of negligence. Is the conscience of the Lord Chancellor to be discarded in favour of the propensities of the reasonable man?

The Court proceeded to consider whether the mortgagee had discharged its duty of care by leaving the sale in the hands of reputable agents. Two of the Lords Justices decided that it was not open to the mortgagee to argue that it had done so because the point had not been taken in the Court below.

However Cross L.J. (as he then was) held that a mortgagee was liable to a mortgagor for any damage suffered by reason of the negligence of the mortgagee's agent. It was put that as a trustee is not liable for the default of an agent whom it is reasonable for him to employ, neither should a mortgagee be. In this respect Cross L.J. said:

But the position of a mortgagee is quite different from that of a trustee. A trustee has not, qua trustee, any interest in the trust property, and if an agent employed by him is negligent his right of action against the agent is an asset of the trust. A mortgagee, on the other hand, is not a trustee and if he sues the agent for negligence any damages which he can recover belong to him.\(^{11}\)

It seems clear from this decision that a mortgagee exercising a power of sale will now act in peril if he relies on one valuation or on one expert alone. Indeed, before selling he may be obligated to investigate fully the different uses to which the mortgaged property may be put and to bring these to the attention of prospective buyers.

Finally, in dealing with the *Cuckmere Brick Co.* case, I should note that *Kennedy v. De Trafford*, although now explained and distinguished in England, may still despite what I have said be of great persuasive force in this country in the sense in which it was generally understood before the recent English decision. In *Latec Investments Ltd. v. Hotel Terrigal Pty. Ltd. (In Liquidation)*\(^{12}\) three members of the High Court of Australia referred to *Kennedy v. De Trafford* as if it were the leading authority as to the validity of the exercise of

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11 Id. at 649.
mortgagees' powers of sale. They did so without any of the qualifications now imposed by the Court of Appeal.

A mortgagee selling should also bear in mind the decision of the Privy Council in *McHugh v. Union Bank of Canada*, if the mortgaged property is at all perishable or liable to be damaged. In that case, the mortgagee sold a mob of horses which realised a depreciated price because of the negligent manner in which the horses had been driven to market. The mortgagee was obliged to account for the difference between the price realised and what a fair price would have been.

LESS FINAL REMEDIES

(a) ENTRY INTO POSSESSION

Entry into possession by a mortgagee has never been a favourite remedy because of the personal liability which a mortgagee assumes and the very onerous duties to account for his receipts and management which are imposed by the court. Despite this many current securities are written on the basis that entry into possession is a possible and indeed likely remedy and the powers of the mortgagee if he does enter into possession are set out at length.

In practice I have never come across the case of a mortgagee entering into possession.

(b) RECEIVERSHIP

I have devoted some time to this topic because so far as I am aware there is no available text on the subject which is entirely suitable for Australian conditions. The English authority Kerr on Receivers must be viewed with caution for reasons which I will mention shortly. In addition it is devoted largely to appointment of receivers by the court and not to appointment out of court. In my experience the great majority of receivers under securities are appointed out of court.

The Law of Property Act confers power on a mortgagee in certain circumstances to appoint a receiver of the income of the mortgaged property and sections 65 and 66 of the Act relate to the operations of such a receiver. However, my remarks are intended to apply primarily to the position of a receiver appointed under an equitable mortgage or under a debenture trust deed. Such appointments are becoming increasingly common. In the first place there has been an increasing

tendency for all operating businesses to incorporate to take advantage of the principles of limited liability. For some years it has been unusual to search against any company and not find it has executed an equitable mortgage in favour of its bankers to secure advances. Such an equitable mortgage invariably authorises the appointment of a receiver upon default and enumerates wide powers for a receiver so appointed.

With respect to bigger corporations it is now less common to find equitable mortgages in favour of their bankers because generally speaking the banking system has not been able to provide all the finance required by expanding major corporations. Consequently bankers have in many cases released equitable mortgages and either lent unsecured to their major customers or taken debenture stock by way of security ranking pari passu with other debenture stock issued by that corporation under a debenture trust deed. It is the position of receivers appointed under such equitable mortgages or debenture trust deeds (and thus out of court) that I wish particularly to consider. After an appointment is made the problems of the secured creditor in enforcing payment of the secured debt become the problems of the receiver.

The problems confronting a receiver can only properly be understood if the position of the receiver appointed in these circumstances is understood. The classical statement of the position is contained in the judgment of Rigby L.J. in *Gaskell v. Gosling*.\(^{14}\) Although this was a dissenting judgment in the Court of Appeal it was unanimously upheld by a strong House of Lords,\(^{15}\) and has recently been described as a masterly statement.\(^{16}\)

Rigby L.J. pointed out the problems confronting a mortgagee in possession to which I have referred briefly above and continued:

> The Courts also favoured any means which would enable the mortgagee to obtain the advantages of possession without its drawbacks. Mortgagees began to insist upon the appointment by the mortgagor of a receiver to receive the income, keep down the interest on encumbrances, and hold the surplus, if any, for the mortgagor, and to stipulate often that the receiver should have extensive powers of management. Presently mortgagees stipulated that they themselves should in place of the mortgagor appoint the receiver to act as the mortgagor's agent. This made no difference in the receiver's position, and imposed no liability

\(^{14}\) [1896] 1 Q.B. 669.
\(^{15}\) [1897] A.C. 575.
on the mortgagee appointing. Though it was the mortgagee who in fact appointed the receiver, yet in making the appointment the mortgagee acted, and it was the object of the parties that he should act, as agent for the mortgagor.\textsuperscript{17}

The deed under consideration by Rigby L.J. provided that the receiver appointed should be the agent of the mortgagor and it is now well settled that provided these words are included in a debenture a receiver will be the agent of the mortgagor so that the mortgagor will not incur liability by his actions. In addition Rigby L.J. made it clear that by virtue of making such an appointment the mortgagor does not become a mortgagee in possession.

However, although he becomes an agent of the mortgagor a receiver does not usurp all the functions of a mortgagor company's board. The directors continue to have powers and duties. In \textit{Hawkesbury Development Co. Ltd. v. Landmark Finance Pty. Ltd.}\textsuperscript{18} Street J. in the course of dealing with an argument that the rule in \textit{Foss v. Harbottle} could not be applied because the company was in receivership said:

There are directors of Landmark Finance currently in office. . . Receivership and management may well dominate exclusively a company's affairs in its dealings and relations with the outside world. But it does not permeate the company's internal domestic structure. That structure continues to exist notwithstanding that the directors no longer have authority to exercise their ordinary business-management functions.\textsuperscript{19}

For this reason he found that the appointment of a receiver did not fetter the power of the directors to institute proceedings in the name of the company challenging the debenture under which the receiver had been appointed.

Finally, although under an equitable security such as I am considering a receiver may be appointed of the whole of the undertaking and assets of a company, nevertheless the company's "equity in redemption" remains untouched. The legal title will remain in the mortgagor, the mortgagee will have an equitable interest by reason of the equitable security and the mortgagor, by reason of his right to redeem and restore to himself full beneficial ownership, will have what members of the High Court of Australia have recognised as an equity of redemption or right in the nature thereof. On appointment the

\textsuperscript{17} [1896] 1 Q.B. 669, 691.
\textsuperscript{18} [1969] 2 N.S.W.R. 782.
\textsuperscript{19} Id. at 790.
receiver will not take control of this equity of redemption. Thus, in *Commissioner of Taxation v. Card* (which I will discuss later) McTiernan J. pointed out that the company's equity of redemption was not part of the company's property of which in that case Mr. Card was receiver and manager. Taylor J. said:

In the case of bankruptcy the property which passes to the trustee in bankruptcy is the property of the bankrupt and, in the case of a winding-up, the property, control of which passes to the liquidator, is the property of the company. If, in either case, the assets which would otherwise be affected are subject to a mortgage, the "property" which will vest in the trustee in bankruptcy or which will pass to the control of the liquidator will be the interest of the company in the mortgaged assets. But in the case of a receiver control of the interest of the mortgagor does not pass to him and in no sense can he deal with it. It may, perhaps, be said, in a general sense that the physical control of the mortgaged assets passes to him but it passes to him only for a very limited purpose, that is for the purpose of enabling him to satisfy the mortgagee's debt. This, in no sense, represents an assumption of control over the mortgagor's interest in the assets. In such a case the property of the mortgagor is not, in law, the property in an unencumbered state; it is the property, subject as it is to the mortgage and it constitutes an interest somewhat in the nature of an equity in redemption.

(i) The receiver as vendor

Under the terms of an appointment of receiver the receiver will invariably have both a power to carry on the business of a mortgagor and a power to sell mortgaged property. He may pursue both courses at the same time.

There is so far as I am aware, no authority similar to the *Cuckmere Brick Co.* case which relates to the obligations which must be observed by a receiver in conducting a sale of mortgaged property. As I mentioned before, in a common law mortgage where a mortgagee is exercising a power of sale he is selling the legal estate which he already holds and the mortgagor's equity of redemption. In the case of a sale by a receiver the assets which the receiver is selling are somewhat different. If the charge under which he has been appointed was a floating charge which became fixed on his appointment or if it was both a fixed and floating charge, the legal estate in the assets being sold remains in the chargor, because the chargee gets only an equitable

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21 Id. at 190.
security. Consequently a receiver exercising a power of sale is selling (a) the legal estate owned by the mortgagor, (b) the equitable estate owned by the mortgagee and (c) the mortgagor’s “equity of redemption” referred to by McTiernan and Taylor JJ. in Card’s case. This he is able to do by virtue of the terms of the deed originally made between the mortgagor and the mortgagee.

This being so it does not seem to me that there is any reason why a receiver in exercising a power of sale should not be subject to the same restraints as a mortgagee exercising a power of sale and with the attendant problems I have already mentioned, including those arising from the Cuckmere Brick Co. case. I think it would be prudent in practice so to advise a receiver. Support for this view can be found in the decision in R. v. Board of Trade22 where it is clear that the Court thought that though a receiver and manager is primarily obliged to serve the interests of the debenture holder, he still has duties to preserve so far as is possible, the goodwill and property of the company.

However this decision does not sit easily with the decision in Airlines Airspares Ltd. v. Handley Page Ltd.23 In this case the Handley Page company had agreed to pay a royalty of £500 in respect of every aircraft of a type known as Jetstream which it sold. The plaintiff company was the assignee of the benefit of this contract. The receiver in effect sold the Jetstream business to a subsidiary company and then sold that subsidiary company to American interests. The plaintiff sought to restrain this action.

The Court held that where a receiver had made it clear he did not in any event intend to continue a contract entered into by a company with a third party, and where the repudiation of the contract would not adversely affect the realisation of its assets or seriously affect its future trading, the receiver was in a better position than the company itself and could frustrate the contract in circumstances where the company itself would not be entitled to do so. Graham J. pointed out that the action of the receiver would render the company liable for damages and might also to some extent damage its reputation as a trustworthy company which could be expected to honour its contracts. He thought however that the sale was in the best interests of all creditors and that any restraint of it would be to favour one creditor at the expense of others.

It can perhaps be said that the decision in the *Handley Page* case is not inconsistent with the view that a receiver must deal gently with the mortgagor's equity of redemption. It seems to assume that a receiver has some duties to the creditors generally. This is to be expected, for if a receiver has duties to the company of which he is a receiver, *a fortiori* he would be expected to have duties to its unsecured creditors who rank ahead of the shareholders in the company in any event.

These unsecured creditors may be represented by a provisional liquidator or a liquidator of the company appointed either before or after the appointment of the receiver. If a liquidator is appointed after a receiver is appointed thereupon the position of the receiver as agent of the company ceases. Whether a receiver thereupon automatically becomes an agent of the mortgagee is problematic but with a liquidator breathing over his shoulder as it were his position becomes far less comfortable. A receiver appointed after a winding-up order is made will almost certainly be appointed as the agent of the mortgagee under the terms of the deed authorising his appointment.

If the assumption is correct that the receiver owes duties of some kind to the unsecured creditors then it will obviously be prudent for a receiver to confer with a liquidator on matters relating to the disposal of substantial assets and seek his concurrence in the course of action proposed if possible. If he cannot obtain such concurrence then if he has any doubts the receiver should surely take advantage of the provisions of section 188 (3) of the Companies Act which entitles him to apply to the court for directions in relation to any matter arising in connection with the performance of his functions.

(ii) *Receiver carrying on business*

The principal problem here is the receiver's position in relation to contracts with the company whether existing at the time of his appointment or entered into by him after that time. Here the position of a receiver appointed out of court contrasts sharply with a receiver appointed by the court. The latter is always personally liable on contracts made by him as receiver, subject to his right to be indemnified out of the property subject to the charge under which he was appointed.

The relevant statutory provisions in Australia are different from the present statutory provisions in the United Kingdom. There, under section 369(2) of the 1948 Act, for almost all practical purposes the position of a receiver appointed out of court by a debenture holder is assimilated to that of a receiver appointed by order of the court.
This was a radical change in the law.\textsuperscript{24} In the United Kingdom as a result of section 369(3) of the 1948 Act a receiver whether appointed by the court or out of court is personally liable under all contracts into which he enters unless the contract otherwise specifically provides. For this reason English texts and authorities since 1948 should be used with caution in regard to the position of receivers appointed out of court in Australia.

The Australian statutory provisions do not in terms go nearly as far as the United Kingdom Companies Act 1948. The relevant provision of the Western Australian Act is section 188 (1) which provides as follows:

Any receiver or other authorised person entering into possession of any assets of a company for the purpose of enforcing any charge is, notwithstanding any agreement to the contrary, but without prejudice to his rights against the company or any other person, liable for debts incurred by him in the course of the receivership or possession for services rendered goods purchased or property hired leased used or occupied.

The sub-section in the New South Wales 1936 Act similar to this sub-section was considered by Street J. (as he then was) in \textit{Associated Newspapers Ltd. v. Grimston}.\textsuperscript{25} In that case the judge was concerned with a pre-receivership contract for the printing and supply to the company of certain magazines, delivery of which had not taken place at the time of the appointment of the receiver. He held that there was no conduct on the part of the receiver showing any intention to pledge his personal credit or otherwise to be a party to the novation of the existing contract.

Though the matter is not entirely free from doubt if the contract does not fall within the scope of section 188 (1) the present position of a receiver appointed out of court appears to be:

(a) in the absence of terms or conduct showing an intention on the part of a receiver to pledge his personal credit or become personally liable, a receiver appointed out of court as the agent of the company is in no way personally responsible in respect of liabilities which may arise out of a contract for sale by the company of property or the performance by the company of work. This applies whether the contract was made by the receiver


\textsuperscript{25} (1949) 66 \textit{W.N. (N.S.W.)} 211.
himself or existed prior to his appointment. This type of contract is clearly not within the terms of section 188 (1). With regard to matters such as defects in the carrying out of work and subsequent maintenance, the other contracting party’s rights (apart from possible set-off) are merely to sue the company. In the event of a successful action against the company the other contracting party would accordingly rank merely as an unsecured creditor.

(b) Where a receiver in the course of carrying on a company’s business enters into fresh contracts of the type within section 188 (1) (that is, for debts incurred or services rendered goods purchased or property hired, leased, used or occupied) he will be personally liable in respect of those contracts subject to his right of indemnity out of the assets of the company.

(c) It is not clear whether section 188 (1) applies to uncompleted pre-receivership contracts or services to be rendered by the company over which the receiver was appointed. The expression ‘incurred by him’ would appear to indicate that the section does not apply to contracts of this type unless the receiver undertakes personal liability by novation or otherwise.

(iii) Set-off against a receiver

Under the general principles of set-off this right applies only where the claims of both sides are liquidated debts or money demands which can be ascertained with certainty. Further the claim must be mutual.

In the case of a receivership the relevant date for determining questions of set-off is not the date of execution of the floating charge but the date of its crystallisation. If prior to the crystallisation of a charge a company has in its trading activities conferred a right of set-off such set-off will survive the appointment of the receiver.

The position is very different in relation to debts arising after the floating charge has crystallised. Debts in favour of the company arising as a result of conduct of the company’s business after the appointment of a receiver out of court as agent of the company can not be set-off against pre-receivership debts owed by the company to the debtor. This is because after crystallisation debts owing to the company as they arise are subject to the company’s equitable charge in favour of the debenture holder. In other words there is no mutuality between the debt arising after the receivership, fixed as it is with the crystallisation of the charge, and a debt owed by the company to the same person prior to the receivership.
(iv) **The problem of preferential debts**

Under section 196 of the Companies Act where a receiver is appointed on behalf of the holders of any debentures of a company secured by a floating charge then, if the company is not at that time in the course of being wound up, debts which in every winding up are preferential debts and are due by way of wages, salary, annual leave or long service leave, and any amount which in a winding up is payable pursuant to section 292(3) or 292(5) of the Act, shall be paid out of assets coming into the hands of the receiver in priority to any claim for principal or interest in respect of the debentures, and shall be paid in order of priority prescribed under section 292. This section causes a number of difficulties of construction and legislative intention. The section applies only where the company is not in the course of being wound up at the time the receiver is appointed. If the company is being wound up at the time of the appointment of the receiver or if subsequent to the appointment of a receiver a winding-up order is made the provisions of section 292(4) operate. It should be noted however that those parts of sections 196 and 292(4) which refer to the debts to be paid in priority are not identical.

By virtue of section 196 the receiver is under a duty to preferential creditors of the type mentioned. He must pay them out of the assets coming into his hands. Consequently it would seem that if the receiver realised moneys but subsequently lost them in the course of carrying on business he could be personally liable to the preferred creditors.

Another matter to note in relation to section 196 is that it applies only where the debenture holder was secured by a floating charge. If the debenture holder was secured by both a fixed and floating charge then the proceeds of realisation of the property subject to the fixed charge are not available to the preferred creditors.

The relationship between section 196 and section 292 was exhaustively considered by the High Court in *Stein v. Saywell and Others.* This case indicates (as does the question of set-off referred to above) how important it may be to determine the exact time that a floating charge crystallises. The facts were complicated but the relevant sequence was as follows.

On the 13th August 1965 a petition to wind up a company called Carapark Industries Pty. Ltd. was filed. Saywell was appointed pro-

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visional liquidator. On the 24th August that year Saywell was appointed receiver under a fixed and floating charge contained in a debenture and subsequently paid out the holder of that debenture from the proceeds of the fixed charge. The appointment of Saywell as receiver made the moneys immediately payable under a second equitable charge by way of floating security which provided that the charge should become a fixed and specific charge upon the moneys secured by such deed becoming payable. Saywell was appointed receiver under the second floating charge on the 11th November 1965 and on the 22nd November 1965 a winding up order was made.

The Court had to consider whether there were in fact any accrued entitlements to employees under the relevant Acts and having decided that there were went on to consider the provisions of section 292(4). This section provides that so far as the assets of a company available for payment to general creditors are sufficient to meet any preferential debts specified in paragraphs (b) and (d) of sub-section (1) of the section, those debts shall have priority over the claims of holders of debentures under any floating charge created by the company and shall be paid accordingly out of property comprised in or subject to that charge. (Paragraphs (b) and (d) relate to wages and annual leave and long service leave respectively.)

The Court held (with Barwick C.J. dissenting) that section 292(4) does not give priority to debts specified in section 292(1) (b) and (d) over claims of debenture holders under charges originally floating which had crystallised prior to the winding up order. McTiernan and Menzies JJ. (with Barwick C.J. again dissenting) further held that section 196 does not apply where the receiver was appointed on behalf of a debenture holder secured by a charge originally floating which had crystallised before the appointment of the receiver.

McTiernan and Menzies JJ. observe that every floating charge would of necessity crystallise at the latest upon the making of a winding up order, for the essence of such a charge is that it is over the assets of a going concern. A floating charge might however survive the commencement of a winding up (that is, the presentation of the petition to the court), for it is quite usual to specify that the making of a winding up order will cause a floating charge to crystallise.\(^{28}\) The dicta of their Honours is consistent with the decision in *Wallace v.*

\(^{28}\) Contrast the position under s. 302 of the Bankruptcy Act under which it is no longer permissible to provide that a secured debt will immediately become payable if an act of bankruptcy is committed.
Automatic Machines Co. Ltd.\textsuperscript{29} where it was held that if a debenture issued by a company by way of floating security contains a covenant for payment of the principal money on a specified day, then without any stipulation making the money immediately payable in the event of a winding up, the occurrence of a winding up before the specified day renders the money immediately payable. There is not however, it is submitted, any essential connection between the fact that the moneys secured by a debenture become immediately payable and the crystallisation of the charge securing them, although in many cases both events will happen simultaneously.

Kitto J. in Stein's case held that for the purpose of section 292(4) the position must be looked at at the time of the making of the winding up order even though the order effectively dates back to the date of the presentation of the petition. If the floating charge had crystallised prior to the winding up order the sub-section did not apply.

In his dissenting judgment Barwick C.J. said:

It is quite clear to my mind that the legislature in enacting these sections did not intend that the priority which it accorded to such debts as those due to employees for wages or accrued leave should be defeated by the circumstance that the floating charge had become crystallized before the time had arrived for determining and giving effect to that priority. The policy behind s. 196 and s. 292(4) is, I think, quite plain. A creditor who accepts a floating charge over a company's assets allows the business of the company to be carried on and the assets of the company which are subject to the floating charge to be altered, perhaps augmented, by the efforts of the company and its employees. The holder of the floating charge is not to be able to displace the priorities which the legislation accords certain debts which accrue during the carrying on of the business; amongst those priorities is certain remuneration of employees of the company.\textsuperscript{30}

Accordingly he held that section 292(4) will come into play if the claims of the chargee to assets or their proceeds arise out of a security which initially created a floating charge which, having become specific, now comprises those assets.

From the point of view of fairness to the company's employees there seems to be a lot to be said for the Chief Justice's views. Indeed the New South Wales legislature has included in the recent amending Act, which received the Royal Assent on 15th December 1971, provisions amending sections 196 and 292(4) with the apparent intention

\textsuperscript{29} [1894] 2 Ch. 547.
of vindicating those views. The reference in these sections to a floating charge is amplified as including 'a charge conferring a floating security at the time of its creation which has become a fixed or specific charge'. Presumably one reads 'has become' as referring to the character of the charge at any time when reference to it is made in these provisions. This would mean that sections 196 and 292(4) would apply to floating charges which had become fixed prior to the appointment of the receiver or making of the winding up order as the case might be.

At the time of writing this paper I know of no corresponding amendment in Western Australia.

However, the New South Wales Act as amended still speaks only of what initially was a floating charge. If the trustee for debenture holders had in the original security the advantage of a fixed charge over part of the company's assets then, as I have indicated and now even with the amended sections 196 and 292(4), there would be certain assets available to the trustee free from preferential claims under those provisions. Perhaps this will not escape the eye of the parliamentary draughtsman here. On the other hand, the considerations of policy mentioned by Banvick C.J. in the passage set out above, as making it reasonable to subject the holder of a charge created as a floating charge, to priorities arising in favour of certain debts accruing during the carrying on of a business, may not favour treating in the same way the holder of what was created as a fixed or partly fixed charge.

(v) A problem with the Commissioner of Taxation

It is not uncommon experience where receivers are appointed to find that prior to the appointment of the receiver substantial moneys have been collected by the company in group tax but not paid over to the Deputy Commissioner of Taxation. I am aware that despite the decision in Card's case referred to above the Commissioner is apt to demand from the receiver payment of these moneys. However it follows from Card's case that the receiver is under no liability to make such a payment, at least until the debenture holder has been satisfied.

In Card's case the receiver was appointed under a bank equitable mortgage. The company was then indebted to the Commissioner of Taxation in the sum of some £3,000 in respect of deductions made from the wages of employees. The receiver realised all the company's assets but these were worth only some £1,400.

Section 221P of the Income Tax Assessment Act provides that where an employer makes a deduction and fails to deal with the
amount so deducted in the manner required by the Act he shall be liable, and where his property has become vested in or the control of his property has passed to a trustee, the trustee shall be liable to pay that amount to the Commissioner.

The majority of the High Court held that the section was not to be construed as imposing any liability on a trustee to answer for the employer's debt to the Commissioner except out of property belonging to the employer which had vested in him or vested under his control. The only property of the company consisted of a worthless equity of redemption and this, in any event, did not vest in the receiver. There was thus never any property of the company which vested in the receiver and out of which its obligations to the Commissioner could be met. In other words the receiver was entitled to realise assets and to pay the debenture holder and only if there was a surplus in his hands after such payment was he obliged to meet the Commissioner's claim.

On the other hand McTiernan and Taylor JJ. took the view that the section in any event did not apply to a receiver, since the section is designed to operate only in the case of a trustee in whom property becomes vested or to whom control of that property passes for the purpose of some form of general administration and that a receiver is not such a trustee. As I have already indicated, in their view the equity of redemption, even if valuable, would not have vested in the receiver.

The same view was taken by Street J. in Re Carapark Industries Pty. Ltd.31 (which case on appeal later became Stein v. Saywell). He said:

But if the individual who is said to be a trustee having control does not have authority to make payments out, in the sense of making distributions, as distinct from meeting current commitments, then it does not seem to me that s. 221P should be regarded as applying to him.32

Consequently on the basis that receivers have no authority to make distributions generally but merely authority to pay the limited proceeds of a receivership to the debenture holders any claim on a receiver under section 221P should be resisted. If after the receiver has paid out the debenture holder and all other costs and expenses incidental to the realisation of the security he finds himself in control

32 Id. at 171.
of assets of the company he may be accountable direct to the Commissioner, though in the view of McTiernan and Taylor JJ. and Street J. he is not.

(vi) Indemnity

As has been pointed out before, a receiver carrying on business is entitled to be indemnified out of the assets of the company subject to the charge under which he was appointed. It is not uncommon, immediately on an appointment being made, for a receiver to carry on business for a period at least to enable him to assess whether the business of the company should be closed down or continued. He may not be sure whether in fact the company is operating profitably but he will not wish to make a hasty decision. At the same time he may be worried that if the state of the company is worse than he thinks its assets may not be sufficiently substantial to provide a comfortable indemnity.

In these circumstances a receiver should and will no doubt ask for an indemnity from the mortgagee or trustee appointing him. However, my experience is that trustee companies at least will be extremely wary and uncomfortable about giving such an indemnity. Very often these companies are not of great substance and difficult practical problems can emerge. The attitude of the trustee is likely to be that the major debenture holders should give the indemnity and this has on occasion been agreed.

If after the receiver has been appointed a winding up order is made so that the receiver is no longer the agent of the company it seems clear beyond doubt that the mortgagee or trustee appointing him should give or arrange an indemnity because, as he is no longer agent of the company, the receiver's right of recourse to the company's assets is lost. A receiver in such circumstances will usually cease all business operations and merely sell off the assets of the company concerned in the best possible way.

PROBLEMS OF THE DEBENTURE UNDER WHICH THE RECEIVER IS APPOINTED

I should like briefly to refer to the point I originally made that many of the problems of a secured creditor (and through him a receiver whom he may appoint) stem from the terms of the original security document. In this regard I would like to make some general comments about the drafting of debenture trust deeds which are so commonly in use today and to such a large extent in standard terms.
(1) Debenture trust deeds have become extremely sophisticated documents which attempt to deal with almost every contingency. In view of the heavy incidence of stamp duty it is not surprising that they depart in form substantially from the precedents set out in Palmer where, as a general rule, they were intended to secure a fixed sum only. After payment of this sum, presumably the deed would have been discharged and if the company wished to borrow further, a fresh deed would have been executed. Modern deeds are designed to be open ended and continuing securities. That is to say, the intention of the company is to issue debenture stock and to redeem such debenture stock in accordance with its terms of issue, and before or after such redemption to issue further debenture stock subject only to the observance of whatever ratios are included in the debenture trust deed. Consequently the first problem of a receiver is very often to determine whether the whole of the stock on issue has in fact been validly issued. Debenture trust deeds commonly contain complicated machinery and conditions precedent which must be satisfied by a company before further stock can be issued. The consequences of failure to observe such conditions precedent are indicated by the decision of the High Court in State Superannuation Board v. Trustees Executors and Agency Co. Ltd.\(^3\) In that case the company did not obtain an appropriate auditor's certificate before issuing stock to the State Superannuation Board and the Court held that the stock issued did not rank pari passu with other stock and indeed that the State Superannuation Board was not a secured creditor at all. Consequently it is essential that the provisions relating to the issue of original stock and further stock should be clear and unambiguous.

(2) Another problem may emerge in relation to the issue of further stock. It is well established that if a first mortgagee makes further advances to his mortgagor after he receives notice of a second mortgage, the first mortgage becomes security only for the amount due at the date of the notice. Further advances by the first mortgagee will thereafter only rank as a third mortgage: Deeley v. Lloyds Bank.\(^3\) What is the position if a trustee gets notice of a second floating charge over the whole of the company's undertaking and assets during the currency of a trust deed? If further stock is issued after such notice is received is such further stock still first mortgage stock or is it third mortgage stock? The facts are not entirely analogous to those which would apply to the bank overdraft with which Deeley v. Lloyds Bank

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\(^3\) [1912] A.C. 756.
is concerned because a trustee is interposed and because the persons
taking the further debenture stock (that is, the persons making the
further advances) may well be different from the persons who originally
took debenture stock. There will no doubt be a leading case on
the subject one day but in the meantime I think it is a wise precaution
to ensure that there are no further charges if acting for an investor
taking up stock or a banker lending on its security.

(3) As has been seen in relation to the doctrine of set-off and in
relation to cases such as Stein v. Saywell, it may be extremely im-
portant for a receiver to know when the floating charge under which
he is appointed in fact crystallised. Often it is clear from a deed when
the moneys thereby secured become immediately repayable. As I have
said before I do not think that this necessarily amounts to the same
thing as the crystallisation of a floating charge. In my opinion in the
absence of anything in a debenture trust deed to accelerate crys-
tralisation of a floating charge, even though the moneys secured by the
deed have become immediately repayable, the floating charge will
only crystallise when the receiver is in fact appointed. It seems there-
fore prudent to insert into debenture trust deeds clauses to the effect
that the floating charge will crystallise when the moneys secured by
the deed become immediately payable. Here again the drafting must
be carefully watched because this may be an undesirable situation.
The position can be safeguarded if the deed contains a clause to the
effect that the moneys will only become immediately repayable at the
option of the trustee. If this is done they will not, for example, become
immediately repayable if there is an inconsequential breach of cov-
enant or a failure to pay interest to a trustee by the due date. There
would have to be some positive action by the trustee, presumably a
notice to the company that the moneys had become immediately pay-
able because of some default. Such notice could at the same time
indicate that the floating charge has simultaneously crystallised.

(4) Further in relation to debenture trust deeds there seems to be
much to be said against the current practice whereby the sole security
taken by the trustee is a floating charge. Bank equitable mortgages
commonly provide that the equitable charge should be fixed as regards
all land buildings and other immoveables and should be floating only
as regards the other assets comprised in the charge. It is hard to see
in the case of most trading companies that such a fixed charge could
operate to the company’s disadvantage. In the event that the fixed
assets of the company are sold during the currency of the charge
(which they would not be very often) there should be little trouble
in obtaining a release by the trustee of the assets being sold if this is necessary.

(5) Finally, I should mention the appointment of two or more persons as receiver. This sometimes is done under trust deeds which contain no clear power enabling this to be done. Further, any express provision in the trust deed should clearly specify that such an appointment is to be joint, several, or joint and several. If this is not made clear, then I believe the presumption to be in favour of all appointments being joint and this may be contrary to what is desired.

A CASE OF NEVER GIVE UP HOPE

There are not many practitioners who will have avoided confrontation with the problems of money lending legislation and the dire consequences of non-compliance with its requirements. The recent case of Congresbury Motors Ltd. v. Anglo-Belge Finance Co. Ltd.\(^3\) shows that even when confronted with an apparently desperate situation all hope should not be abandoned. In this case a registered money lender agreed to lend a garage proprietor a substantial sum to buy a service station, the loan to be secured by a legal mortgage over the freehold of the business. The note or memorandum required by the English legislation was not made and the contract for the repayment of the moneys lent and the mortgage were unenforceable under the provisions of that legislation. However, the moneys lent had been paid by the finance company direct to the vendor who had sold the service station to the borrower. This, I think, would be a fairly normal occurrence in money lending transactions involving the purchase of goods or businesses.

In these circumstances the Court of Appeal held that by application of the doctrine of subrogation the lender was entitled to the vendor's lien over the property purchased for the money which the lender had paid to the vendor. The Court of Appeal was prepared to assume that there was a moment of time between the completion of the purchase and the completion of the mortgage and held that this was sufficient for the lender to become subrogated to the vendor's lien and that the acceptance of the legal mortgage did not waive or abandon or supersede or cause a merger of the lien. Further, and this

\(^{3}\) [1970] 3 All E.R. 385; the implications of this case in relation to, for example, *ultra vires* borrowings by corporations, are considered in (1971) 34 M.L.R. 207; the discussion of general principle may be compared with that in the Victorian decision of Evandale Estates v. Keck, [1963] V.R. 647, which was not cited to the Court of Appeal.
is a point of general importance and interest, they held that the appli-
cation of the doctrine of subrogation did not conflict with the policy
of the legislature for the protection of the borrowing public. The
equitable doctrine survived the impact of the statute and mitigated
inequitable consequences of its application.

It will be surprising if this case does not in the future provide some
comfort for money lenders who omit to adhere to the strict require-
ments of the various money lending Acts or more likely to their solici-
tors who through inadvertence or otherwise fail to observe or under-
stand some of their perplexing intricacies.

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