Paul McQuade QC (PM): Welcome everyone to Level Twenty Seven Chambers' 'Insolvency Law Update - Badenoch and the End of the Peak Indebtedness Rule'. The Full Federal Court decision of *Badenoch [Integrated Logging Pty Ltd v Bryant]* was delivered in May of this year. Most of you may know that the decision brings to an end the peak indebtedness rule. However, there are other important issues in this decision, and which will be dealt with in the presentation today in addition to the indebtedness rule.

You will take away from this presentation what *Badenoch* said about the running account, the doctrine of ultimate effect for claim preferences and the continuing business relationship in addition to the peak indebtedness rule. You are also obtain an update on the current state of the law in relation to the set off defence in unfair preference claims.

There will be two questions which we endeavour to answer today: how do practitioners know how to frame and prepare a running account defence? And what is the current state of the law in relation to the set off defence in unfair preference claims given its controversial history?

The speakers for this presentation are Mr. Sean Russell and Ms. Hannah Lilley who are members of Level Twenty Seven Chambers.

Mr. Russell practices in the area of commercial litigation and has particular experience and interest in matters concerning bankruptcy and corporate insolvency law, contracts, equity, professional negligence and the Corporations Act. Notably, he is a joint author of an article 'Unfair preferences: Putting an end to the peak indebtedness "rule"' in August 2016. Mr. Russell is well placed to present today in relation to the issues raised in relation to *Badenoch*, as to the running account, the doctrine in ultimate effect, continuing business relationships and the peak indebtedness rule.

Next, Ms. Hannah Lilley will be presenting on the availability of the set off under s 55C of the Corporations Act in relation to defence to a preference client, which was also mentioned in *Badenoch*. Ms. Lilley has a civil and commercial practice. She previously worked at major legal firms both in Australia and in London. Her focus has been on arbitrations, commercial litigation, and regulatory investigations.

Just pausing there, before we commence the presentation, just reminding viewers who are online. If you look to the bottom of your screen, there is a chat button. You can utilise that chat button to put forward any questions you may wish to ask and they will be identified. Also, the recording of this presentation will be uploaded as soon as it is possible.

I invite Mr. Sean Russell to commence the presentation. Thank you.

Sean Russell (SR): Thank you Paul and good afternoon everybody. The area of the topic that I am going to address is the principal importance of the decision of the Full Court in *Badenoch* which is the abolition of what came to be known as the "peak indebtedness rule". It is a rule which has its origin in the bankruptcy legislation and from a case called *Queensland Bacon Pty Ltd v Rees* from the 1960s, which we will come to shortly.

588FA(3) - IMPORTANCE OF RUNNING ACCOUNTS TO PROVE A CONTINUING BUSINESS RELATIONSHIP

[Slide 3]

SR: But what we should commence with, as we always should in statutory interpretation, is the text of the legislation itself. Those of you familiar with this area of the law will know that section 588FA(1) deems transactions which give a preference to creditors voidable. There are of course other provisions where nominating them as insolvent transactions and then voidable transactions. But for present purposes, what we are concerned with is subsection 588FA(3) which incorporates and picks up the language of many of the older cases about the running account. Here, we will see, the language changes slightly in the focus of the core of the section it is on the continuing business relationship between debtor and creditor, of which a running account is given in the legislation as one example.

There are a few problems with the drafting of the section. His Honour Justice Young described the section in *Liquor Administration Board* as "verbose and difficult to comprehend", which is about as close as you will get to a judicial comment saying "it's a dog's breakfast". Because there are many elements to the drafting of the section, which if one were unconstrained by authority, raise more questions than they answer.

For present purposes, what you need to establish is the existence of a continuing business relationship throughout the period, the relation back period between the company and the creditor of the company. That particular transaction is an integral part of that relationship. Then, in the course of the relationship, the level of the company's net indebtedness is increased in use from time to time. And that the fluctuation in the net indebtedness is a result of a series of transactions forming part of the relationship.

[Slide 5]

One of the examples about the difficulties with the draft legislation is that in subsection (b), the fluctuation in the indebtedness does not have to be an integral part of the continuing business relationship. There are lots of little problems like that in the drafting that have not necessarily been picked up in any of the cases but which may or may not continue into the future.

In any event, once those matters and s 3 are established, then subsection (c) and (d) take effect, which is that all of the transactions which form part of the relationship together

constituted a single transaction. And that any particular transaction under consideration is that then only a preference if all of the transactions taken together as the single transaction is itself a preference. There are two important things about that. The first is that because it modifies s 1, it is strictly understood to be an element of the cause of action, rather than as it is sometimes referred to the running account defence. Understanding that helps understand why the Full Federal Court altered the previous understanding of how the rule operated. Because jumping ahead a little bit, what the Full Court said in *Badenoch* is that it is open to the liquidator to prove from any point going forward that a transaction ceases to be an integral part of the continuing business relationship, or that in fact the continuing business relationship has come to an end and that what is happening is really a reduction in the overall indebtedness. But it is not open then to define for themselves when the continuing business relationship is taken to have commenced.

HISTORICAL RELIANCE ON DOCTRINE OF ULTIMATE EFFECT – *AIR SERVICES AUSTRALIA*

[Slide 6]

SR: Also important in this context, and something the Full Federal Court placed a great deal of reliance on is the last time that the High Court had occasion to look at unfair preferences, the case of *Air Services Australia*. Now, it was not itself a peak indebtedness case but the underlying principles applicable to unfair preferences help understand what has happened with the indeptedness rule. And that is, the High Court espoused in this case what has come to be known as the doctrine of ultimate effect. You will see one formulation of it on the screen.

[Slide 7]

There is another passage from the judgment in which the majority said "If at the end of a series of dealings, the creditor has supplied goods to a greater value than the payments made to it during the period the general body of creditors are not disadvantaged by the transaction, they may even be better off. Consequently, a debtor does not prefer a creditor merely because it makes a regular payment under an express or tacit arrangement. That while the debtor makes the payments, the creditor will continue to supply goods." In such a situation the court does not regard the individual payments as preferences, even though they are unrelated to any specific delivery of goods and services and may ultimately have had the effect of reducing the amount of indebtedness of the debtor. If the effect of the payments is to reduce the initial indebtedness, only the amount of the reduction will be regarded as a preferential payment. And that is without recourse to the text of the Act, the essential basis of the running account defence. That is, it was once thought prior to the establishment of the running account defence that you could cumulatively treat each payment along the way during the relation back period as though it were a separate preference. As liquidators often do in the absence of a continuing business relationship, you just total up all the payments during the period. But where the payments are made in an effort to obtain further supply, it's necessary, the High Court says, to consider the ultimate effect of all of the transactions.

WHAT IS A CONTINUING BUSINESS RELATIONSHIP AND HOW DO YOU ESTABLISH ONE?

SR: What is a continuing business relationship? And how can you as practitioners go about establishing one? *Badenoch* is useful in this sense, as well, in that in paragraph 48, their Honours put together a very helpful list of the sorts of things and the principles that apply to the proof of the existence of a continuing business relationship, remembering that that is a question of fact, in any unfair preference claim. What needs to be established is that the payment is made in circumstances where there is a mutual assumption of a continuing relationship of debtor and creditor with an expectation that further debits and credits will be recorded. That is, it is not a problem for the creditor when the creditor says, "Look, Mr. Debtor, your account is out of order. If I'm going to keep supplying to you with goods, in order for you to continue to trade, you must make some payments down to the debt." That is the essence and the example which is seen all the time as being evidence of a continuing business relationship. In doing so, there are a number of authorities which say that it is usually relevant to consider a Statement of Account in determining, from a business point of view, whether each particular payment was connected with the subsequent provisions of goods or services. You will often have a body of evidence which includes both communication between the creditor and debtor companies, and often in larger organisations the debt collection part or the financial side of the business chasing payment of old invoices. But it is also important to take a look at the Statement of Account to look at the credits and debits along the way from which it might be inferred that the continuing business relationship is either continuing or has come to an end. For example, if you were to look at a Statement of Account and there ceased to be debits to the account representing a supply of goods, it becomes easier to infer that from that point on the continuing business relationship has ceased because no further goods were supplied and so you would follow ordinarily that there was not a mutual assumption that further goods would be supplied.

Importantly, if the purpose of the payment is to induce the creditor to provide further goods or services, as well as to discharge an existing indebtedness, the payment will not be a preference unless the payment exceeds the value of the goods or services acquired. It is only the extent to which, and we will come to some graphical representations of this in a moment, any payment reduces the overall preexisting level of indebtedness at the start of a six month period where it is an integral part of a continuing business relationship that it can be considered a preference.

Where the relationship contemplates further debits and credits, that is the running account rule applies, the appropriation of a payment to a past debt is not unusual and has no significance unless the parties expressly agree that one of the purposes of the payment is to permanently reduce through one of the purposes of the payment is to permanently reduce the level of indebtedness below the level existing at the time of the agreement. Often, you will see what happens in practice is the businesses apply payments, particularly lump sum

payments, simply to their oldest invoice. In principle, there is no reason to treat that any differently. In the absence of some express agreement, saying this payment is for the purpose of reducing prior indebtedness, in which case, the proper statutory analysis would probably be that it is not an integral part of the continuing business relationship because it is not a payment made to induce further supply.

Importantly, a stop on an account does not necessarily destroy a continuing business relationship. That is one of the features that liquidators often point to, if a customer is placed on stop supply, that will suggest but not definitively determine the end of the continuing business relationship.

And finally, as with many aspects of the law, it is a question of substance and not form.

You can see from those principles in relation to establishing the necessary parts of s 3, (a) and (b), that it can be quite a factually intensive inquiry. Often, defendants to an unfair preference claim will run with good faith defences. And the evidence, I would imagine, as is often the case, there will be quite a degree of overlap between the evidence which relates to the suspicion of insolvency that the creditor may have had, and the evidence which establishes the existence of the continuing supply and the continuing business relationship, the purpose of the payments which are the subject of the transaction.

PEAK INDEBTEDNESS RULE & CORPORATIONS ACT – THE END?

[Slide 8]

SR: Within that context of running accounts, is the peak indebtedness rule, which has its origin in this statement of Chief Justice Barwick from *Queensland Bacon v Rees*. This is the limit of the analysis which formed the basis of the rule. It was a case in which the liquidator had done what liquidators always do, which is to take the most advantageous position and plead peak indebtedness. There was some criticism of that in the case and the Chief Justice said, "No, no, that's fine."

[Slide 9]

In the context of the old statutory language, that might have been right, but the way that 588FA is structured, there is simply no warrant for it. That is one of the things that the Full Federal Court said in *Badenoch*. There was a line of authorities to the effect that because the Corporations Act, this part of the Corporations Act, was not intended to change the law as it related to unfair preferences and simply to codify that the peak indebtedness rule should be taken to have survived the enactment of the Corporations Act. But the first reason is that there is no textual support at all for the peak indebtedness rule in 588FA(3). That was the first of the three reasons that the Full Court pointed to in *Badenoch*. The second and third are closely related and go to ultimately, why is it in terms of policy and purpose behind these provisions

that a liquidator should be permitted to select the point of peak indebtedness as the measure of the preference.

[Slide 11]
Returning to the language of the Act, reminding ourselves. Once these qualifications have been met by reference to the principles and evidence that we' have been discussing a moment ago, the consequence is this, all the transactions forming part of the relationship are considered together. There is nothing in that language which says only part of the transactions. It is a directly contrary reading of the plain language of the Act. What the Full Federal Court said in *Badenoch* would be to read the section in accordance with the peak indebtedness rule would be to sever the single transaction and not create a single transaction to which s 1 applied but two transactions, one before and one after the point of peak indebtedness which, as I have said, for which there is no support in the language of the Act.

[Slide 14]
So, we go back to s 1. The second reason has to do with the doctrine of ultimate effect, which is that the purpose of unfair preference provisions is to prevent any creditor from obtaining an advantage over another by reason of these payments in the dying days of an insolvent company. What happens is, the payment is made in order to secure further supply. The overall position of creditors is not worse off because, assuming that there is nothing untoward about the price paid for the goods, the company receives goods of an equal or greater value than what they paid for. And so, the general body of creditors receives the benefit of the company having those goods being available to the liquidator for sale in the winding up of the company and the proceeds of sale being available to be distributed to the other unsecured creditors.

One way of visualising it, as appears on the screen, is if you were to consider the overall asset position of a company at the point in time of any particular payment. The amount of cash on hand of the company decreases as a result of the transaction but the amount of goods that the company has available to satisfy the claims of its creditors increases and so that many times there will not be any overall change in the asset position of the company and therefore no preference to the particular creditor in having received a payment in exchange for the provision of goods. Now, that the purpose of the policy level is the basis of the doctrine of ultimate effect. It neatly sidesteps the problem that in a winding up the goods on hand are often sold for less than the price paid by the company or for fire sale prices. That is said in a policy and purpose of sensitivity irrelevant to the application of the rules.

[Slide 15]
The third reason is that the stated purpose of part 5.7B of the Act which deals with voidable transactions is to promote fairness in the treatment of unsecured creditors. The peak

indebtedness rule has the ability to work in very unfair ways, depending upon the particular circumstances of the company and the account in question.

We are going to look at three examples, which are taken from an article referred to by the Full Courtin *Badenoch* and in each of these examples, a normal trading relationship safe a widget, the creditor has a gift as a $10,000 credit limit for the supply of goods. At the beginning of the six month period, there is an indebtedness of $10,000. The creditor provides $60,000 worth of goods in the six months and the debtor company pays $60,000 for those goods. Applying the literal language of 588FA it can immediately be seen that the single transaction has not resulted in any overall reduction to the company's indebtedness over the six month period. On that theory, there should be no preference. [Slide 16] But, assume that each month there is a $10,000 supply and a $10,000 payment. On that analysis, even assuming that the last payment is made in the expectation of further debits and credits to the account, which can often not be the case. You know, in the very last days of an insolvency, it is not uncommon for the final payments to not have any real expectation of future trade. But assume that, to be for the purposes of this example, the peak indebtedness theory would allow for a preference of $10,000 in relation to that last payment. Whereas the competing, I will say that they are competing but they really ought to be considered together, but the competing theory of ultimate effect is that there is no preference because the commencement of the period the company was indebted $10,000 at the end of the period was embedded in a sum of $10,000.

In our second example, assume that there is a series of supplies of the first three months of $20,000, then one large payment, followed by a resumption of $10,000 a month in supply $10,000 in payment. Here, the peak indebtedness theory would have a preference of $20,000, despite the overarching single transaction having been unchanged.

[Slide 17]
The final example has is one where there is a very great deal of supply, a small payment, some more supply and a large payment. This is something that I would suggest is not uncommon in commercial terms, in that somebody gets on credit and there is a great deal of supply and as well as a small payment to induce further supply then a large payment. In this case, because the peak indebtedness is $60,000 and closing indebtedness is $10,000, there is a $50,000 preference.

In each of these cases, the doctrine of ultimate effect, applying the language of the statute, as a single transaction has no preference reported. But the peak indebtedness rule produces three different results depending merely on the timing of the supplies and the payments which the Full Court has said generates unfairness between unsecured creditors treated on an equal footing because one unsecured creditor might face a very large preference claim and another one might face one that is not a preference claim at all. When you step back and

consider the purpose of the provisions, what has happened, taking these transactions all together, is that the general body of creditors is no better or worse off as a result of the transactions because there has been an identical level of payment and goods supplied. So to the extent that the payments have been made, they have been met by the provision of goods which are available to the payment of the other unsecured creditor's debts.

Those were really the core reasons behind the Full Court's reasoning in *Badenoch*. I recommend that you have a look in the future, particularly at the section involving the first issue in the case, which was the continuing business relationship. It is a very helpful analysis of factually what needs to be identified in order to establish those things because you can see in accordance with the principle that one looks at the Statement of Account. Even from this point, it might be in fact possible to say that the very large payment that occurs towards the end of the period was not as an integral part of a continuing business relationship at all, but having regard to the communications passing between the parties, whatever letters of demand might have been going out, that in fact the continuing business relationship had ceased, and not withstanding that there was a further supply. When the payment was made, there was not a mutual expectation that the continuing business relationship would continue. It remains a question of fact in each case, having regard to the principles that were set out helpfully in *Badenoch*. But now, by reference to the language of the Act, rather than the practice that had developed out of liquidators applying that peak indebtedness rule, which now no longer forms part of the law. That being said, the other issue of the case which Hannah will turn to, which remains live is the question of mutual credits and set offs in relation to unfair preferences claim. So I will hand over to Hannah to deal with that issue.

MUTUAL CREDITS AND SET OFFS IN RELATION TO UNFAIR PREFERENCE CLAIMS

[Slide 19]

Hannah Lilley (HL): Thanks Sean. Good afternoon everyone.

Badenoch also argued that the primary judge erred in not finding that it was entitled to set off the amount still owing to it by Gunns against any amount the Court found it liable to pay the liquidators for its unfair preference pursuant to s 553C of the Act. With respect to that issue, the Full Court held that the primary judge had correctly identified that Badenoch was not entitled to set off because it had notice of facts that would plainly support a conclusion that Gunns was insolvent. It was therefore unnecessary to determine whether as a matter of law the court may permit the use of set off to reduce Badenoch's liability to make any payment ordered by the court because of an unfair preference.

That is an unfortunate outcome in relation to the set off point. It has for some time been the point of much controversy, especially in light of justice Edelman's discussion in *Hussain v CSR Building Products Ltd* in 2016, and Justice Gleeson's discussion in *Re RORCE CORP PTY LTD (in*

liq) in 2020. Both cases which I will discuss shortly. However, in both *Hussain* and *Re FORCECORP*, it was also unnecessary for the court to decide on the matter of set off as it was in *Badenoch*.

Taking a step back, we will have a look at the actual section. S 553C of the Corporations Act provides for a statutory set off between an insolvent company and a person who wants to have a debt or claim admitted against the insolvent company. As can be seen from its terms, section 553C is alive and when there are mutual credits, mutual debts or other mutual dealings between an insolvent company the person who wants to have the debt or claim admitted provided that the person did not have notice of the fact that company was insolvent when it gave credit to the company or received credit from the company.

3 REQUIREMENTS FOR SET OFF TO TAKE PLACE

[Slide 20]

HL: As such, there are three requirements which must be satisfied before a set off can take place.

First, the respective claims must exist at the commencement of the winding up, that is the date for determining what claims are admissible to proof against the insolvent company.

Secondly, the respective claims must be commensurable. That is mutual credits, debits or other dealings must be found in money as opposed to for example, a claim for specific performance. And there must be mutuality as between the respective claims. The same person must be both prosecuting a claim and responding to a claim. The equitable and beneficial interests of the parties must be the same. The person cannot be prosecuting and responding to a claim in different capacities. For example, there will be no mutuality if a person is prosecuting a claim as a trustee or partner responding to a claim and his own personal capacity.

Mutuality does not require that the respective claims be contractual or correspond to one another, nor does that require that claims be identical or the same, but rather, it indicates reciprocity that there are reciprocal claims by the insolvent company on one hand and the creditor on the other.

[Slide 21]

By way of example of how a set off claim can work example:

- Company A supplies $100 of goods to Company B;
- Company B makes a car payment of $60 to Company A; and,
- Company B goes into liquidation;

- The liquidator claims $60 payment from Company A has an unfair preference; and,
- Company A sets off the $40 still owing to it and only pays back $20;
- The $40 that was set off set off is then treated as a secured debt in the insolvency and the remaining $60 is admitted as proof of insolvency.

The converse of this is if set off were not permitted is that Company B would have to return the part payment it received to the liquidator and lodge a proof of debt for the full $100. In doing so, depending on the funds available and distribution after various expenses and secured debts are paid out, the creditor may receive for example 40 cents on the dollar for the full $100. Whereas applying the set off over here, the creditor receives its $40 and then would get 40 cents on the dollar for the remaining $60 which it would lodge as proof of debt.

So, permitting set off in this manner is very much in favour of that particular creditor but not so much the rest of the creditors seeking their distributions. It reduces the pool of funds available to them and is therefore contrary to the purpose which the statutory insolvency claims given.

AUTHORITIES ON SET OFF

[Slide 22]

HL: The relevant line of authority on the availability of set off in these circumstances are set out on the slide. So *Re Parker* decided in 1997 includes perhaps the most comprehensive analysis of the availability of set off. In that case, Justice Mansfield allowed a set off claim to recover the payment from a holding company which was based on insolvent trading.

Then in 1997, in *Hall v Poolman* Justice Palmer allowed a set off to liquidator's insolvent trading claim against a director of the company.

In 2011, the conclusion in *Re Parker* was considered in the context of voidable transactions in *Buzzle Operations Pty Ltd v Apple Computer Australia*. In that case, Justice Young with whom Justices Hodgson and Whealy agreed, held to payments made by Buzzle to Apple Computer were uncommercial transactions. The set off defense did not need to be considered in that case because the good faith defense applied. However, *in obiter*, Justice Young appeared to extend the application of s 553C to uncommercial transactions as well.

But in 2015, there were two relevant decisions. The conclusion in *Re Parker* was applied by the in the Federal Court by Justice Gleeson in *Smith v Boné*. And in *Morton & Anor v Rexel Electrical Supplies Pty Ltd* Justice Sales held that set off applied to an unfair preference claim in the District Court of Queensland feeling constrained to apply Justice Young's *in obiter* in Buzzle.

Then in 2018, in *Stone v Melrose Cranes & Rigging Pty Ltd* Justice Markovic followed the decision in *Re Parker* and *Buzzle* and *Hall v Poolman*, and how that set off can be used in voidable transaction claims for an unfair preference.

[Slide 23]
These judgments have been the subject of quite a lot of criticism. The biggest academic criticism is by Dr. Rory Derom in his article published in 2015. In that article, he wrote that the line of authority favouring the view that set off may be available against claims under s 500C were wrongly decided, as a matter of principle, and that set off should not be available for three reasons: they are contrary to the statutory purpose of claims being to benefit unsecured creditors; there is a lack of mutuality; and, the statutory claims do not arise until after the time determining the available availability of set up in the liquidation and not therefore properly characterised as contingent at the relevant time.

In relation to the lack of mutuality in particular, Dr. Derom argued that the company, while not a trustee, would not be properly characterised as the beneficial owner of the statutory insolvency claim. That is because prior to liquidation, the company could not charge or assign the claim as future property, nor could it give an effective release in relation to any such claim in a future liquidation. The claim is given for the benefit of others, the company's creditors and the company could not deal with that as its own and the company is therefore not a beneficial owner in this sense, which the expression is being referred to. And so, if the company is not the beneficial owner of a statutory insolvency claim in a winding up then there should be no mutuality in relation to that claim and a separate debt owing by the company to the defendant the purpose of a set off between those parties in liquidation.

So in *Re FORCE CORP*, Justice Gleeson referred to Dr. Derom's criticisms expressing his view that there is much force in the detailed analysis and criticisms. And Justice Edelman also referred to Dr. Derom's article in *Hussain,* although because he was not required to determine the point of set off in that case, he did not consider the critique any further.

THE AVAILABILITY OF UNFAIR PREFERENCE CLAIMS
[Slide 24]
HL: Why does this matter? Liquidators running unfair preference claims are no doubt already alive to the potential for defendant to raise a claim under s 553C on the back of decisions such as *Buzzle* and *Stone v Melrose Cranes*. However, the ongoing criticisms of those rulings, particularly as reinforced by Justice Gleeson in *Re FORCE CORP*, may well provide the impetus for a liquidator to seek appellate level review of the area of law should an appropriate and sufficiently commercial opportunity arise. Indeed, one of those has arisen recently. So the question of set off under s 533C and it's availability to a defendant as a defence was brought before Justice Derrington in a case management hearing on the 24th of March of this year

[2021], where he reserved the question for consideration of the Full Court, which I believe is to be heard later this year. That is in the case of *Gavin Morton as liquidator of MJ Woodman, Electrical Contractors and Metal Manufacturers*.

WHAT INSTRUCTIONS OR EVIDENCE DO PRACTITIONERS NEED FROM CLIENTS TO ESTABLISH A RUNNING ACCOUNT DEFENCE?

PM: Thank you very much Sean and Hannah for your presentation.

Before we identify any questions that may have been put through by online viewers, I have just got a question for Sean in relation to his presentation. What instructions or evidence do practitioners need from clients to establish a running account defence?

SR: Thanks Paul. There's nothing like a Dorothy Dixer.

The sorts of things that you should be looking for are the same sorts of things that you would ordinarily look for in a good faith defence. There would be a particular emphasis in accordance with the principles of the Statement of Account. So, making sure that all of the supplies and payments are properly documented, and that the invoices that were sent through were paid. The second aspect to it is those communications which occur between creditor and debtor. And what they say about one, in fact, whether the payments were made. The primary purpose that needs to be established on a running account defence, that is in order to secure further supply. Or, as is often the case, in the absence of express evidence about that, whether in the totality of the circumstances they were made on the mutual assumption of the continuing debits and credits to the running account. It is in one sense, as it always is, impossible to define the factual limits that might bear upon those questions but ordinarily you will be looking at the fact of the supplies and the payments, and what communications occur, often in larger organisations between the finance team and the debtor and the business side, which will often say "Yes, that's fine. We'll keep supplying as long as you make a few payments". So that could be very helpful evidence of what you need to establish on a continuing business relationship case.

PM: Thank you very much.

WHY HAVE JUDGES BEEN RELUCTANT TO ENGAGE CRITICISMS OF LAW REALTING TO UNFAIR PREFERENCE?

PM: I have also got a question for Hannah if she doesn't mind me asking this. Why do you think judges have been reluctant to engage the criticisms of the law in relation to a claim for settling unfair preference?

HL: Thank you, Paul.

It is often the case that because parties very commonly run a good faith defence in these sorts of claims which means that the evidence of knowledge of insolvency is inevitably led at trial and where that evidence exists it is open to the court to make a finding on fact under s 553C without having to address whether as a matter of law the statutory insolvency claims can be set off under s 553C. Then after *Buzzle* was handed down, the Court of Appeal made that decision whilst the comments on the availability of set off were made *in obiter* and single judges have felt bound to follow that sense. That is why Justice Derrington has referred that point on a preliminary issue to the Full Federal Court, which means they will have to engage with that question as a matter of law without having seen the facts yet.

PM: Any questions from the audience? Does anyone here? I know there might be some online. Does anyone physically present have any questions for either Sean or Hannah?

PAYMENTS TO A LOAN ACCOUNT

Audience: What evidence would be put to show that loans to a shareholder, not a director of a company, but then goes into liquidation are not unfair preference?

SR: For those that might not have heard online, the question is about payments on a loan account. I think the anterior question will be the more difficult one, which is to establish that the loan account is part of a continuing business relationship. The expressions in the Act, an integral part of a continuing business relationship, are taken from older judgments relating to the ongoing supply of goods and services being secured by the payment. Standing here, it is difficult to imagine a circumstance in which it will be proper to characterise a loan account as relating to the ongoing supply of goods and services, in that necessarily, very often, the shareholder's loan account will be for the purposes of supplying operating capital to the business rather than in exchange for any goods or services. If you take it back to the fundamental principle being the doctrine of ultimate effect, the body of creditors is worse off as a result of payments on a loan account because there is not a correlative asset in the nature of goods and services which they have received, which can be applied for their benefit in the ultimate winding up of the company.

PM: No further questions then?

Thank you very much for your attendance today at our seminar. We look forward to your future attendance in our seminars. I would like you to put your hands together, for those that are present today, to thank Sean and Hannah.