

Article Information

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The Importance of DIRRIs has been highlighted

In February 2014, we published an Insolvency Update discussing the matter of *Re Walton Constructions Pty Ltd (in liq)*; *ASIC v Franklin [2014] FCA 68*

In February 2014, we published an Insolvency Update discussing the matter of Re Walton Constructions Pty Ltd (in liq); ASIC v Franklin [2014] FCA 68, in relation to an unsuccessful application by ASIC to remove the liquidators of the relevant companies for a perceived lack of independence and impartiality (also seeking further declarations that the DIRRI they completed was deficient).

ASIC appealed the decision to the Full Court of the Federal Court of Australia. The appeal concerned two main issues (set out below)

On 18 July 2014, the Full Court unanimously:

- Upheld ASIC's appeal to the extent Messrs Franklin, Horne and Stone (Liquidators) be removed as liquidators of Walton Construction Pty Ltd (in liq) and Walton Construction (Qld) Pty Ltd (in liq) (the Companies) (the First Issue).
- Dismissed ASIC's appeal to the extent that ASIC claimed that the primary judge erred in holding that the Liquidators, when acting as administrators of the Companies, did not contravene section 436DA of the Corporations Act 2001 (the Act) (the Second Issue).

The First Issue

Our February 2014 article sets out the background which is relevant to this matter.

In concluding that there was a conflict which is more than theoretical that may affect the Liquidators properly discharging their duties as liquidators, Justice White (Justices Jessup and Robertson agreeing):

- Considered that the applicable test to be applied is the "double might" test stated in *Ebner v Official Trustee in Bankruptcy*
- Concluded that ASIC had established that the reasonable fair-minded observer might consider that the Liquidators had an interest which conflicted with their duties.
- Considered that the fair-minded observer would know that it would be commonplace for proposed administrators or liquidators to meet company directors before their appointment, and that those meetings often included the provision of preliminary advice to the distressed company.
- Agreed with ASIC's submission that the Referrer appeared to have influenced the selection of the persons who, as liquidators, would investigate their own pre-administration conduct. It would be natural for the fair-minded observer to think that the Referrer regarding the Liquidators as being possibly more amenable to its interests than other might be.
- Thought that a reasonable fair-minded observer might reasonably apprehend that, because of the Liquidators' interests in not jeopardising future income, they might not discharge their duties with independence and impartiality.

Such a finding resulted in the Full Court ordering that the Liquidators being replaced – despite the fact they had been appointed several months earlier, and that such a change to liquidators at this point in time would cause considerable expense, delays and inconvenience to the liquidation.

The Second Issue

In concluding that the Liquidators did not breach section 436DA of the Act, Justice Robertson (Justices Jessup and White

agreeing) agreed “with the primary judge to the extent that her Honour said that the need to investigate the [Referrer] was a matter pertaining to the performance of the administrators’ duties and did not objectively add anything further as to the existence of the association with the [Referrer]”.

The Full Court also made comments about the Insolvency Practitioners Association of Australia’s (now known as ARITA) guide entitled *Code of Professional Practice for Insolvency Practitioners*, on which ASIC relied, as material which was appropriate to be taken into account in construing ss 60 and 436DA of the Corporations Act.

The Full Court determined that, general law would not permit that guide to be taken into account in construing those provisions and that the guide was outside the scope of the *Acts Interpretation Act 1901* (Cth).

Summary and consideration

Accordingly, it appears that the Full Court accepted ASIC’s position that the failure to complete the DIRRI and disclose the referral relationship was enough that a reasonable fair-minded observer might reasonably apprehend a conflict which should result in the removal of the Liquidator. But the Court determined that the conflict was not sufficient to amount to a breach of section 436DA of the Act.

Liquidators ought take note of this decision where they are referred matters in which they may be required to investigate the conduct of that referrer and/or make investigations that may result in voidable transactions affecting the referrer to ensure they will not be deemed to be in conflict and thus risk being removed along the track.