

When and how can a liquidator 'disclaim property of the company'?

Susan Cirillo reports on *Willmott Growers Group Inc v Willmott Forests Limited (Receivers and Managers Appointed) (In Liquidation)* [2013] HCA 51

Say a company in liquidation is the landlord under a long-term lease and the tenant has fully paid rent in advance: What if, before the end of the term of the lease, the company's liquidator wants to sell the company's interest in the land without the encumbrance of the lease?

According to a majority (4:1) of the High Court, the liquidator can disclaim the lease pursuant to s 568(1) of the *Corporations Act 2001* (the Act). The tenant loses its right to exclusive possession of the land and is required to prove for its losses in the winding up.

Background

Willmott Forests Limited (Willmott) owned or leased land which it then leased to the participants of forestry investment schemes to grow and harvest trees (the growers). Each lease to the growers was for a term of generally 25 years and some included a renewal option. Some leases required the rent to be fully paid in advance rather than periodically.

Willmott's liquidators negotiated contracts to sell Willmott's interests in the land which it owned or leased unencumbered by the leases to the growers. The liquidators applied for directions and orders from the court under s 511 of the Act in respect of those negotiated contracts.

In the Supreme Court of Victoria, Davies J, as matter for preliminary determination, found that although the liquidators were able to disclaim the growers' leases, this did not have the effect of extinguishing the growers' leasehold estate or interest in the subject land. The liquidators successfully appealed to the Court of Appeal. A body representing the growers appealed to the High Court.

The relevant provisions

Section 568(1) of the Act gives a liquidator power to 'at any time, on the company's behalf...disclaim property of the company that consists of' any of six enumerated categories of property, of which, relevantly sub-paragraph (f) refers simply to 'a contract'.¹

A liquidator cannot disclaim a contract (other than an unprofitable contract or a lease of land) except

with the leave of the court: s 568(1A).

From its date of effect, disclaimer terminates the company's rights, interest, liabilities and property in or in respect of the disclaimer property, and only affects any other person's rights or liabilities so far as necessary in order to release the company and its property from liability: s 568D(1).

A person aggrieved is taken to be a creditor of the company to the extent of any loss suffered because of the disclaimer and is allowed to prove that loss as a debt in the winding up of the company: s 568D(2).

The majority's reasons

The majority (French CJ, Hayne and Kiefel JJ; Gageler J writing separately) dismissed the growers' appeal.

The growers had argued that the liquidators could only 'properly' disclaim Willmott's reversionary interest in the leases, that is, the estate in possession that reverts to Willmott, as lessor, after the lessee's right to exclusive possession has ceased. Therefore, they submitted that this reversionary interest was a type of property that was engaged by sub-paragraphs (a) and (c) of s 568(1) of the Act, being respectively, 'land burdened with onerous covenants' and 'property that is unsaleable or is not readily saleable'. However, this argument was understood as advancing the proposition that leases are not property of the company for the purposes of s 568(1).

French CJ, Hayne and Kiefel JJ rejected this proposition. Their Honours stated that the reference to 'property of the company' in s 568(1), which conferred a power to 'disclaim' such property, was not confined to the object in respect of which property rights exist, but rather directed attention to the legal relationship which exists between the company and the object, and so it referred to the company's possession of any wide variety of legal rights against others in respect of some tangible or intangible object of property.² Therefore, the reference in paragraph (f) to 'a contract', their Honours said, identified, 'as the disclaimer property, the rights and duties which arise under the contract'.³ Their Honours stated that a lease was a species of contract⁴ and referred to

Deane J's classic description of a lease in *Progressive Mailing House Pty Ltd v Tabali Pty Ltd*, where his Honour said that a lease is both 'an executory contract and an executed demise'⁵. In separate reasons Gageler J, also referring to this description, explained that even where the rent is fully paid, a lease is never fully executed during its term because the lessee maintains an ongoing right to exclusive possession and the lessor has an ongoing obligation to give exclusive possession.⁶

French CJ, Hayne and Kiefel JJ held that the bundle of rights and duties of landlord and tenant under a lease can be identified as a species of property – they derive from the contract of a lease, and therefore, even when it is the company that is the landlord, a lease can be properly described as 'property of the company that consists of...a contract'.⁷

The growers argued, alternatively, that even if s 568(1) of the Act allowed a liquidator to disclaim a company's lease of land to a lessee, then that would not mean that the effect of disclaimer set out in s 568D(1) would destroy a third person's interest in property which existed before the disclaimer. French CJ, Hayne and Kiefel JJ said that it was important to recognise that tenants do not stand as third parties divorced from the rights, interests and liabilities of the company which are to be brought to an end – the company's rights, interests and liabilities in respect of the leases cannot be brought to an end without bringing to an end the correlative liabilities, interests and rights of the tenants.⁸

Gageler J's approach differed from that of French CJ, Hayne and Kiefel JJ. Their Honours considered, as a matter of statutory construction, whether a lease of which the company was a landlord would constitute 'a contract' within the meaning of s 568(1) (f). In contrast, Gageler J appeared to consider the effects of 'disclaimer', by reference to the 'long history of judicial consideration of similar provisions in insolvency legislation'⁹ and then posed the question of whether a lease of which the company is the landlord answers the description of 'property of the company that consists of ... a contract', so as to fall within the power of the liquidator to disclaim.¹⁰

Gageler J observed that disclaimer only operates to release the company from its prospective rights and obligations in relation to the property that is disclaimed, not any liability which the company incurred to another person in relation to the property before the disclaimer took effect, nor an interest in the property which the company transferred to another person before the disclaimer took effect.¹¹ Therefore, a lease cannot be equated to an interest in property which has already been transferred, given that it is contingent upon the ongoing enjoyment of rights conferred by the lease.¹² His Honour essentially found that a lease of which the company was a landlord could be disclaimed pursuant to s 568 because the recognition in s 568D(1) that disclaimed property may include property of which the company has liabilities, as well as rights and interests, effectively enlarged the meaning of 'property' in s 568(1).¹³

Keane J's dissent and the issue of seeking leave to disclaim

French CJ, Hayne and Kiefel JJ noted that it was not necessary to consider whether the liquidators required the leave of the court before disclaiming the leases and what considerations would inform the decision to grant or refuse leave.¹⁴

Keane J would have allowed the appeal and determined that, without the leave of the court under s 568(1A), the liquidators' purported disclaimer of the leases were not effective, but that if the liquidators were to successfully apply for leave to disclaim the leases, then only Willmott's ongoing obligations to the growers would be terminated. His Honour held that Willmott could not seize possession of the land contrary to the rights which have 'accrued' to each of the growers.¹⁵ A court of equity would restrain an attempt to deprive the growers (who had paid their rent fully in advance) of their right to possession.¹⁶

On the issue of leave, Keane J concluded that the liquidator could disclaim, without leave, a lease of land in which the company was the lessee (because as his Honour appeared to reason, this power applied in respect of a lease contract that is 'property of the company' which in 'ordinary parlance' would be understood as 'property of the lessee'¹⁷), but that if

the company was the lessor, the liquidator would require leave to disclaim pursuant to s 568(1A).¹⁸ His Honour appeared to query whether the legislature might have assumed that leases in which the company receives rent as the lessor (supposedly like contracts that are the opposite of ‘unprofitable contracts’) are beneficial to the company, hence leave to disclaim is required.¹⁹ Though, in the present case, the liquidators did not share that assumed view.

Practically, one would query why a liquidator would want to disclaim a contract which from the point of view of the company and waiting creditors at least, likely could be described as ‘profitable’. This may suggest that the legislature did not intend that the question of leave be determined by reference to whether a contract is beneficial to the company or not.

In circumstances where the issue of leave has not been fully determined by the High Court and there may be difficulties in determining whether a contract is ‘unprofitable’ within the meaning of s 568(1A), prudence would suggest that if in doubt, leave should be sought (or at least the issue might be canvassed in an application for directions under the Act). On the other hand, practitioners will note that by reason of s 568C, disclaimer takes effect by reference to the notice that the liquidator must give under s 568A, which includes notice to each person who appears to the liquidator to have, or to claim to have, an interest in the property and that s 568E allows such a person to apply, with the leave of the court, for an order setting aside the disclaimer after it has taken effect.²⁰ Depending on the circumstances, issues as to the propriety of a liquidator’s purported

disclaimer may be canvassed, in any event (without leave having been sought pursuant to s 568(1A)), in the course of litigation if an interested party objects to the disclaimer.

Endnotes

1. Subparagraphs (a) to (e) state:
 - (a) land burdened with onerous covenants; or
 - (b) shares; or
 - (c) property that is unsaleable or is not readily saleable; or
 - (d) property that may give rise to a liability to pay money or some other onerous obligation; or
 - (e) property where it is reasonable to expect that the costs, charges and expenses that would be incurred in realising the property would exceed the proceeds of realising the property...
2. [2013] HCA 51 at [35]-[36]. Their Honours noted that this reading was consistent with the Act’s definition of ‘property’ in s 9, as it stood at the time of hearing before the primary judge, i.e., ‘any legal or equitable estate or interest (whether present or future and whether vested or contingent) in real or personal property of any description and includ[ing] a thing in action’.
3. [2013] HCA 51 at [38].
4. [2013] HCA 51 at [39].
5. (1985) 157 CLR 17 at 51.
6. [2013] HCA 51 at [65]-[67].
7. [2013] HCA 51 at [40].
8. [2013] HCA 51 at [54].
9. [2013] HCA 51 at [71].
10. [2013] HCA 51 at [75].
11. [2013] HCA 51 at [71].
12. [2013] HCA 51 at [72].
13. [2013] HCA 51 at [76]-[77].
14. [2013] HCA 51 at [54].
15. [2013] HCA 51 at [134] and [161].
16. [2013] HCA 51 at [157].
17. [2013] HCA 51 at [129].
18. [2013] HCA 51 at [116].
19. [2013] HCA 51 at [133].
20. Only if the court is satisfied that it is unreasonable in all the circumstances to expect the person to have applied for an order setting aside the disclaimer before it took effect.

