CHADWICK INDUSTRIES (SOUTH COAST) PTY LTD v CONDENSING VAPORISERS PTY LTD

FEDERAL COURT OF AUSTRALIA – GENERAL DIVISION

LOCKHART J

18 February 1994 – Sydney

Statutory demand – Setting aside – Whether genuine counter-claim or cross-demand – Standard to which court must be satisfied – Whether frivolous or vexatious claim – Corporations Law ss 459G, 459H(1)(b).

Words and phrases – "genuine claim"

The respondent served a statutory demand on the applicant pursuant to s 459G of the Corporations Law for a debt of $7750, being the balance due under a contract between the parties made in March 1993. The applicant applied to set aside the demand.

The issue was whether the applicant had a genuine counter-claim or cross-demand against the respondent as required by s 459H(1)(b) of the Corporations Law. The applicant claimed that the machine designed and supplied by the respondent under the contract, a prototype platform trolley for materials to handle roofing components, was defective and not suitable for its intended purpose. The applicant claimed that it incurred additional expenses totalling $61,210.84 in rectifying the problems arising from the faulty trolley. The expenses incurred included engineering costs, staff costs, electrification work, access scaffolding, trolley storage and administration costs.

Held, setting aside the statutory demand:

(i) The standard of satisfaction which the court must reach on the question of whether or not there is a genuine offsetting claim is not a particularly high one. The court will not examine the merits of the dispute other than to see if there is in fact a genuine dispute. The notion of a "genuine dispute" in this context suggests that the court must be satisfied that there is a dispute that is plainly not vexatious or frivolous. The court must be satisfied that there is a claim that may have some substance.

> *Mibor Investments Pty Ltd v Commonwealth Bank of Australia* (1993) 11 ACSR 362; *Re Morris Catering (Australia) Pty Ltd* (1993) 11 ACSR 601; *Scanhill Pty Ltd v Century 21 Australasia Pty Ltd* (1993) 12 ACSR 341, applied.

(ii) This was not a case of a frivolous or vexatious claim by the applicant against the respondent. It was one which may or may not ultimately have substance, but on all the evidence, it was a "genuine claim" within ss 459G and 459H of the Corporations Law.

Application

This was an application to set aside a statutory demand made pursuant to s 459G of the Corporations Law. The facts appear sufficiently in the following reasoning for judgment.

P Walsh instructed by *O'Connor Filewood & Co* for the applicant.

P Parsons instructed by *Lassidy Gibson Howlin* for the respondent.

Lockhart J. The application being heard today is to set aside a statutory demand pursuant to s 459G of the Corporations Law. The new regime relating to statutory demands was introduced into the Corporations Law fairly recently. It has been the subject of some judicial comment, including a judgment of mine in *Topfelt Pty Ltd v State Bank of New South Wales Ltd* (1993) 12 ACSR 381, though the precise point that has arisen in this matter did not arise in Topfelt. I there referred to the division at some length and analysed many of its provisions. I need not repeat what I said.

In an application like the one today the court must be satisfied that the applicant has an offsetting claim: s 459H(1)(b). An offsetting claim is defined by s 459H(5) as meaning:

> A genuine claim that the company has against the respondent by way of counter-claim, set-off or cross-demand (even if it does not arise out of the same transaction or circumstances as a debt to which the demand relates).

So, the question for decision today is whether the court is satisfied that the applicant has a genuine counter-claim or cross-demand against the respondent. The expression "genuine claim" has been considered by several judges. It was a question that arose before Hayne J of the Supreme Court of Victoria, in *Mibor Investments Pty Ltd v Commonwealth Bank of Australia* (1993) 11 ACSR 362. His Honour examined the meaning of those words at 366 and 367 and considered them in the light of some five matters to which he referred at 366. It is helpful to repeat what he said because I agree with it:

> . . . any application to set aside a statutory demand must be made very quickly: it must be made within 21 days. Second, the statute contemplates a summary procedure, the only outcome of which will be an order affecting the statutory demand, not an order or judgment declaring a debt to be owing or not to be owing or ordering payment of any money sum. Third, the only significance that the statutory demand has is that if there is a failure to comply with it then the company is deemed to be insolvent. Thus the demand is no more than a precursor to an application for winding up in insolvency. Fourth, an application to wind up in insolvency must be determined within 6 months (unless the court is satisfied that special circumstances justify an extension of that time): s 459R. Fifth, on the hearing of the application to wind up, the company may not oppose the application on grounds that it might have taken in any application to set aside the demand, unless those grounds are material to proving that the company is solvent.

His Honour said that:

> These matters, taken in combination, suggest that at least in most cases, it is not expected that the court will embark upon any extended inquiry in order to determine whether there is a genuine dispute between the parties and certainly will not attempt to weigh the merits of that dispute. All that the legislation requires is that the court conclude that there is a dispute and that it is a genuine dispute.

The point was also considered by Thomas J in the Supreme Court of Queensland in *Re Morris Catering (Australia) Pty Ltd* (1993) 11 ACSR 601 where his Honour said at 605-606:

> There is little doubt that Division 3 is intended to be a complete code which prescribes a formula that requires the Court to assess the position between the parties and preserve demands where it can be seen that there is no genuine dispute and no sufficient genuine offsetting claim. That is not to say that the Court

will examine the merits or settle the dispute. The specified limits of the Court's examination are the ascertainment of whether there is a "genuine dispute" and whether there is a "genuine claim".

He went on:

> It is often possible to discern the spurious, and to identify mere bluster or assertion. But beyond a perception of genuineness (or the lack of it) the Court has no function. It is not helpful to perceive that one party is more likely than the other to succeed, or that the eventual state of the account between the parties is more likely to be one result than the other. The essential task is relatively simple – to identify the genuine level of a claim (not the likely result of it) and to identify the genuine level of an offsetting claim (not the likely result of it).

Beazley J considered the matter in this court in *Scanhill Pty Ltd v Century 21 Australasia Pty Ltd* (1993) 12 ACSR 341 at 356-7, where her Honour referred to the passages to which I have just referred in Thomas J's judgment and also to Haynes J's judgment in *Mibor*. Her Honour then went on to propound the appropriate test, for the purposes of s 459H, to determine the correct approach to be made by a court in deciding whether there is a genuine claim.

The test that appealed to her Honour is whether the court is satisfied that there is a serious question to be tried that the applicant has an offsetting claim, a test well known with respect to interlocutory injunctions. Whether her Honour's test is common to all the judgments to which I have referred, may be an arguable question. However, what appears clearly enough from all the judgments is that a standard of satisfaction which a court requires is not a particularly high one. I am for present purposes content to adopt any of the standards that are referred to in the cases: Haynes J's judgment, Thomas J's judgment or Beazley J's judgment. The highest of the threshold is probably the test enunciated by Beazley J, though for myself I discern no inconsistency between that test and the statements in the other cases to which I have referred. However, the application of Beazley J's test will vary according to the circumstances of the case.

Certainly the court will not examine the merits of the dispute other than to see if there is in fact a genuine dispute. The notion of a "genuine dispute" in this context suggests to me that the court must be satisfied that there is a dispute that is not plainly vexatious or frivolous. It must be satisfied that there is a claim that may have some substance. On the other hand the court must be careful, because if all an applicant has to do is to assert both a claim and some basis for it, without more, it would mean in almost every case that the court would set aside statutory demands where application is made to that effect. Plainly that is not what the legislature intended by introducing this new regime.

I turn to the facts. The demand served by the respondent upon the applicant contains in the schedule thereto a description of the amount of the debt which the respondent says the applicant owes him. The amount is some $7750 and it is said to arise from a contract between the parties made in March 1993, the amount of the contract being $24,500. The amounts that have been paid by the company are said to be $16,750, leaving a balance due from the applicant to the respondent of some $7750.

There is some evidence of dispute as to the precise amount that has been paid by the applicant to the respondent, but nothing seems to turn on that

for present purposes, as the area of dispute is fairly fine, the applicant saying it has paid $17,655.60, a difference of roughly $1000. The applicant claims that under a contract made on 17 March 1993 it agreed with the respondent for the respondent to design and supply a prototype platform trolley for materials to handle roofing components on the roof of a building to be constructed and known as the Aquatic Centre at the Homebush Bay Olympic Centre, for a price of $24,500.

It asserts that the prototype platform trolley in fact designed and supplied by the respondent was defective and was not suitable for its intended purpose. The applicant says that the defects were such that it required extensive engineering modifications associated with design and checking of the trolley for WorkCover Authority certification and that rectification works were necessary before the trolley could be used for its intended purpose.

The applicant says that, by reason of the alleged default of the respondent, it incurred expenses in employing other contractors and time spent by its own officers and staff in rectifying the problems arising from the alleged faulty design and alleged defective trolley. It also claims it lost the benefit of the moneys it paid to the respondent pursuant to the contract.

The applicant has specified 12 categories of expenditure which it says it has incurred. I need not relate them all; they include engineering costs, staff costs and electrification work, access scaffolding, trolley storage and administration costs. The claim is for $61,210.84.

The evidence in support of the applicant's case leaves something to be desired. I realise it is difficult for a party to prepare its case in a short time and to prepare an affidavit of the kind required by s 459G. It is difficult for a company which alleges faulty design of prototype machinery to organize its case into any proper state in a short time.

The matter came before the court last year and I adjourned it on the applicant's application, because the evidence, as it then stood, was admittedly deficient. I gave directions as to the filing of evidence and affidavits by the parties, and the matter came on today for final hearing. Affidavits were filed by the applicant. However, they suffered from some of the defects of the initial affidavits. I acceded to the request of counsel for the applicant and allowed him to call oral evidence today from Mr Fitzgerald, who is a project manager of the applicant and held that position at all times relevant to this claim.

The evidence as to the contract between the parties, on which the claim of the applicant is based, and the evidence of the alleged defective design of the workmanship and the expense incurred by the applicant totalling its claim of $61,000-odd, is somewhat slight. Nevertheless, last Tuesday, 15 February, albeit at the eleventh hour, it filed in the District Court of New South Wales a statement of liquidated demand where it sets out its claim. In due course the District Court will hear the applicant's case and any motions that may be brought by the respondent with respect to it.

Whether the claim is found to be made out is a matter for the District Court; it is not for this court to determine that matter. There is evidence from Mr Fitzgerald of a kind which, if it is accepted, suggests that there were substantial problems with the prototype platform that may emanate initially from design faults. Whether the defects are ultimately proved to

exist, and if they are, whether they are the fault of the respondent, I do not know, and it is not appropriate to examine that question on an application such as this.

In my opinion, this is not a case of a frivolous or vexatious claim by the applicant against the respondent. It is one which may or may not ultimately have substance; but in the light of the evidence, including Mr Fitzgerald's oral evidence, I am satisfied that there is a genuine claim in the sense in which that expression is used in ss 459G and H of the Corporations Law. Whether the applicant will establish its claim in the District Court, is a matter on which I say nothing. For present purposes, it will be sufficient for the applicant to succeed to say that the claim is one which may be more than $7750, which is the amount of the debt which the respondent is owed by the applicant.

Bearing in mind that the contract value of the machinery was $24,500, it is not beyond the bounds of reality that if there is a claim that is ultimately proved by the applicant, it may be a figure of at least $7750. I must emphasise again that I am not determining the merits of any claim of the applicant against the respondent, nor am I determining the credibility of Mr Fitzgerald's oral evidence; but it was not suggested by counsel for the respondent that he was other than a credible witness.

I should add that s 459H(2) requires the court to calculate the substantiated amount of the demand in accordance with the formula of admitted total minus offsetting total. In this case the admitted total is $6344, the offsetting total would be $61,210.84; but to comply with the section strictly one would have to deduct the larger from the lesser figure, which is a most odd requirement. I doubt if it is one intended by the section in those circumstances, but if it is, then the deduction of the greater from the lesser is the amount of the demand that is required by the sections.

Accordingly, the court orders that the statutory demand served by the respondent upon the applicant on or about 21 September 1993 be set aside.

The question arises as to what should be the appropriate order for costs. On 17 December the Court ordered that the applicant pay the respondent's costs of that day for the reasons which I then gave and need not repeat. The applicant sought an adjournment because its case was not in proper shape. It then had the benefit of directions to file and serve affidavits, but those affidavits were themselves defective. It was not until today, in particular not until Mr Fitzgerald gave oral evidence, that the court was persuaded that there is a genuine claim of the kind to which ss 459G and H is directed.

In all the circumstances, the appropriate order for costs is that the applicant should pay the respondent's costs of the proceeding up to, but not including today, and that there should be no order for the costs of either party of today. Accordingly I make that order.

A P KINNEAR
SOLICITOR