Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd [2008] NSWSC 1344 (11 November 2008)

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NEW SOUTH WALES SUPREME COURT

CITATION:
Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd [2008] NSWSC 1344

JURISDICTION:
Equity Division
Corporations List

FILE NUMBER(S):
2445/08

HEARING DATE(S):
10-11 November 2008

EX TEMPORE DATE:
11 November 2008

PARTIES:
Lemery Holdings Pty Ltd (plaintiff)
Reliance Financial Services Pty Ltd (in liq) (defendant/first respondent)
Reliance Financial Services NSW Pty Ltd (applicant)
Max Christopher Donnelly as Liquidator of Reliance Financial Services Pty Ltd (second respondent)
Anna Theresa Zeiter (third respondent)
Josephine Mizzi (fourth respondent)
Marthas T Market Pty Ltd (fifth respondent)
Francesco Criniti, Caterina Castellano & Josephine Joan Romano (sixth respondent)
Dennis Phillip Griffiths (seventh respondent)
Ghandi Faiz Sobbi & Zaneh Faizi Sobbi (eighth respondent)

JUDGMENT OF:
Brereton J

LOWER COURT JURISDICTION:
Not Applicable

LOWER COURT FILE NUMBER(S):
Not Applicable

LOWER COURT JUDICIAL OFFICER:
Not Applicable

COUNSEL:
Mr M A Ashhurst SC w Mr D A Allen (applicant)
Mr P B Walsh (defendant/first & second respondents)
Mr A F Fernon (third respondent)
Mr T G Feerick (fourth respondent) (sol)

SOLICITORS:
Proctor & Associates (applicant)
Church & Grace (defendant/first & second respondents)
McCabe Terrill Lawyers (third respondent)
Frontier Law Group (fourth respondent)
Macedone Legal (fifth respondent)
Agostino & co (sixth respondents)

CATCHWORDS:
EQUITY – trusts and trustees – trustees right of indemnity – equitable liens – where trustee removed upon winding up pursuant to trust instrument and new trustee appointed – whether causes of action in other proceedings to recover loans are trust assets – whether removed trustee can retain possession of assets to secure indemnity pending determination – whether right of indemnity survives transfer of trust assets to new trustee – whether a removed trustee is entitled to retain assets as against a new trustee to secure its indemnity

LEGISLATION CITED:
(NSW) Trustee Act 1925, s 9
(NSW) Real Property Act 1900
(NSW) Uniform Civil Procedure Rules, r 7.8

CATEGORY:
Principal judgment

CASES CITED:
ANZ Banking Group Ltd v Intagro Projects Pty Ltd [2004] NSWSC 1054
Belar Pty Ltd (in liq) v Mahaffey [1999] QCA 2; [2000] 1 Qd R 477
Chief Commissioner of Stamp Duties for New South Wales v Buckle [1998] HCA 4; (1998) 192 CLR 226
Coates v McInerney (1992) 7 WAR 537
Davies v Littlejohn [1923] HCA 64; (1923) 34 CLR 174
Dimos v Dikeakos Nominees Pty Ltd (1996) 68 FCR 39
Dowse v Gorton [1891] AC 190
Fletcher v Collis [1905] 2 Ch 24
Global Funds Management (NSW) Ltd v Burns Philp Trustee Co Ltd (in prov liq) (1990) 3 ACSR 183
Hewett v Court [1983] HCA 7; (1983) 149 CLR 639
Hillig v Darkinjung Local Aboriginal Land Council [2006] NSWSC 1371
Jennings v Mather [1901] 1 QB 108
Jennings v Mather [1902] 1 KB 1
Kemtron Industries Pty Ltd v Commissioner of Stamp Duties [1984] 1 Qd R 576

Melbourne Tramways Trust v Melbourne Tramway & Omnibus Company Ltd (1887) 13 VLR 487
Octavo Investments Pty Ltd v Knight [1979] HCA 61; (1979) 144 CLR 360
Official Assignee of O'Neill v O'Neill (1898) 16 NZLR 628
Re Akerman [1891] 3 Ch 212
Re Enhill Pty Ltd [1983] 1 VR 561
Re Exhall Coal Co Ltd [1866] EngR 131; (1866) 55 ER 970
Re Paulings Settlement Trust (No 2) [1963] Ch 576; [1963] 1 All ER 857
Re Pumfrey (1882) 22 Ch D 255
Re Stucley [1906] 1 Ch 67
Re Suco Gold Pty Ltd (in liq) (1983) 33 SASR 99; (1983) 7 ACLR 873
Ronori Pty Ltd v ACN 101 071 998 Pty Ltd [2008] NSWSC 246
Savage & Whitelaw v Union Bank of Australasia Ltd [1906] HCA 37; (1906) 3 CLR 1170, 1188
Southern Wine Corp Pty Ltd (in liq) v Frankland River Olive Co Ltd [2005] WASCA 236; (2005) 31 WAR 162
Tennant v Trenchard (1869) LR 4 Ch App 537
Trim Perfect Australia v Albrook Constructions [2006] NSWSC 153
Vacuum Oil Co Pty Ltd v Wiltshire [1945] HCA 37; (1945) 72 CLR 319
Wilson v Parker (1846) 10 Jur 979
X v A and Others [2000] 1 All ER 490
Xebec Pty Ltd (in liq) v Enthe Pty Ltd (1987) 18 ATR 893

TEXTS CITED:
Meagher and Gummow, Jacobs' Law of Trusts in Australia, 5th ed (1997) Butterworths
Sykes & Walker, The Law of Securities, 5th ed (1993) Lawbook Co
Underhill and Hayton, Law of Trusts and Trustees, 16th ed (2003) Butterworths

DECISION:
The loans were trust assets. The former trustee's right of indemnity from trust assets survives the appointment of and transfer of assets to a new trustee. The old trustee cannot retain trust assets against the new trustee to secure its indemnity.

JUDGMENT:

IN THE SUPREME COURT
OF NEW SOUTH WALES
EQUITY DIVISION
CORPORATIONS LIST

BRERETON J

Tuesday, 11 November 2008

2445/08 Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd

JUDGMENT (ex tempore)

1 **HIS HONOUR**: The defendant and first respondent Reliance Financial Services Pty Ltd ("Reliance"), of which in earlier days Mr Sam Cassaniti was the principal, was wound up by order of the Court made in these proceedings on 26 June 2008. Reliance's liquidator, Mr Maxwell Donnelly, is the second respondent to the present application. Reliance is party to seven other proceedings in this Court – some of them in this Division and some of them in the Common Law Division – in which it seeks to recover from third parties loans which it made to them, and which they resist essentially on (NSW) *Contracts Review Act* 1980 and related grounds. Those third parties are the other (third to eighth) respondents to the present application.

2 Pursuant to a Deed of Settlement dated 1 July 1994, Reliance – then known as Reliance Investment Services Pty Ltd – was appointed the trustee of a discretionary trust called the Reliance Discretionary Trust. The appointor was Mr Sam Cassaniti.

3 Clause 13 of the Deed provided:

The appointor may at any time and from time to time by deed or by notice in writing delivered to the trustee remove any trustee hereof in its absolute and unfettered discretion and the right to remove any trustee hereof and to appoint new or additional trustees hereof by deed or notice in writing is hereby vested in the appointor ...

4 Clause 26.2 of the Deed provided:

The office of the trustee should be ipso facto determined and vacated if the trustee shall enter into liquidation or bankruptcy whether compulsory or voluntary (not being merely a voluntary liquidation for the purposes of amalgamation or reconstruction) or if a receiver or official manager shall be appointed of the undertaking of the Trustee or any part thereof.

5 It follows, from clause 26.2, that upon the winding up of Reliance on 26 June 2008, its office as trustee of the Reliance Discretionary Trust was determined and vacated. By a Deed of Appointment, also made on 26 June 2008, Mr Cassaniti appointed Reliance Financial Services NSW Pty Ltd ("RFSNSW") as new trustee in place of Reliance. The consequence is that RFSNSW is now the trustee of the Reliance Discretionary Trust in place of Reliance.

6 Clause 27.1 of the Deed provided as follows:

A trustee shall on retirement or removal take such action as is necessary to vest the Trust Fund or cause it to be vested in any new trustee and shall deliver to such new trustee all books, documents, records and other property relating to the Trust Fund. Until transfer to the new trustee of any property belonging to the Trust Fund the old trustee will hold the Trust Fund as bare trustee for the new trustee.

7 The application presently before the Court is brought by RFSNSW by interlocutory process filed on 25 July 2008, in which it seeks a declaration that it has been appointed as trustee of the Reliance Discretionary Trust; a further declaration that the loans the subject of the various third party

proceedings are assets of the trust and have vested in RFSNSW; alternatively, a vesting order; and, upon an undertaking not to settle the third party proceedings, and to pay any moneys recovered from them into a controlled moneys account, an order pursuant to (NSW) *Uniform Civil Procedure Rules*, r 7.8, giving RFSNSW the conduct of all the third party proceedings.

8 There are two main issues to be decided. The first is whether the causes of action in the third party proceedings, and the loans and securities the subject of those proceedings, are assets of the Reliance Discretionary Trust. The second is, if so, whether the former trustee Reliance is entitled to retain those assets in its possession, notwithstanding its removal and replacement by RFSNSW as trustee, as security for its right of indemnity against the trust assets.

Are the loans, securities and causes of action arising from them assets of the Reliance Discretionary Trust?

9 As to the first issue – whether the loans, securities and causes of action arising from them are assets of the Reliance Discretionary Trust – Mr Cassaniti has given evidence that each of those loans was a transaction made by Reliance in its capacity as trustee of the Reliance Discretionary Trust, using assets of the Reliance Discretionary Trust. Minutes of the Annual General Meetings of the trustee over the years since 1995 record that the trust "continued to trade as an investment vehicle lending moneys to various borrowers". There is evidence indicating that, in about 1995, Mr Cassaniti determined that he would carry on business through the structure of a trust. Notices lodged with the Australian Taxation Office in connection with ABNs indicate that Reliance ceased to trade in its own right in 2000, and thereafter traded only as a trustee.

10 There is no evidence to the contrary. There is no evidence that Reliance entered into the relevant transactions in its own right rather than as trustee. It is true that at no time did Reliance disclose that it was acting as trustee and, in particular, in earlier proceedings in the Court concerning the present fourth respondent Mrs Mizzi, it was not disclosed that Reliance was acting as trustee. But that would have been an irrelevant matter to disclose, and in any event there is no obligation on a trustee to disclose that it is acting in that capacity. Insofar as any land instruments are involved, the (NSW) *Real Property Act* 1900 would not permit disclosure on the face of the register of the circumstance that the registered proprietor was acting as trustee. I do not think that any inference can be drawn, from the circumstance that there was no such disclosure, that Reliance was not acting as trustee.

11 In the absence of contrary evidence, it seems to me that on balance the evidence plainly establishes that the loans, and the causes of action arising from them, are trust assets. Accordingly, the first issue is resolved by concluding that the subject loans, securities and causes of action were held by Reliance in its capacity as trustee of the Reliance Discretionary Trust.

Is the former trustee entitled to retain the trust assets as security for its right of indemnity?

12 I turn then to the second, and much more difficult, issue, which is whether a former trustee, as Reliance now is, is entitled to retain the trust assets as security for its right of indemnity, notwithstanding its removal and replacement by a new trustee.

13 The relevant principles concerning a trustee's right of indemnity against trust assets include the following, for which I am indebted in large part to the analysis by Austin J in *Trim Perfect Australia v Albrook Constructions* [2006] NSWSC 153, [20].

14 *First*, as against a third party, a trustee is personally liable for debts and liabilities incurred in its capacity as trustee [*Vacuum Oil Co Pty Ltd v Wiltshire* [1945] HCA 37; (1945) 72 CLR 319; *Octavo Investments Pty Ltd v Knight* [1979] HCA 61; (1979) 144 CLR 360, 367].

15 *Secondly*, however, the trustee has a right of indemnity out of the trust assets for expenses or liabilities incurred by the trustee, by recoupment of expenditure and exoneration from liability [*Octavo Investments*, 367; *Chief Commissioner of Stamp Duties for New South Wales v Buckle* [1998] HCA 4; (1998) 192 CLR 226, 245].

16 *Thirdly*, this right of indemnity, recoupment and exoneration is secured by an equitable lien over the trust assets, which arises by operation of law and confers a proprietary interest, in the nature of a security interest, in the trust assets, and takes priority over the claims of beneficiaries [*Octavo Investments v Knight*, 367, 370; *Chief Commissioner of Stamp Duties v Buckle*, 246].

17 *Fourthly*, this equitable lien extends to all of the trust assets, save only those that are specifically excluded by the trust instrument [*Dowse v Gorton* [1891] AC 190; *Octavo Investments v Knight*, 367].

18 *Fifthly*, being an equitable lien, the security is enforceable by the trustee only by judicial sale or appointment of a receiver, and not by foreclosure nor by sale out of Court [*Tennant v Trenchard* (1869) LR 4 Ch App 537; *ANZ Banking Group Ltd v Intagro Projects Pty Ltd* [2004] NSWSC 1054, [14]; *Melbourne Tramways Trust v Melbourne Tramway & Omnibus Company Ltd* (1887) 13 VLR 487, 490; *Re Pumfrey* (1882) 22 Ch D 255, 265; *Re Stucley* [1906] 1 Ch 67; *Davies v Littlejohn* [1923] HCA 64; (1923) 34 CLR 174, 184; *Hewett v Court* [1983] HCA 7; (1983) 149 CLR 639, 663; Sykes & Walker, *The Law of Securities*, 5th ed, (1993) Lawbook Co, 198].

19 *Sixthly*, the right of indemnity accrues at the time the obligation is incurred [*Xebec Pty Ltd (in liq) v Enthe Pty Ltd* (1987) 18 ATR 893; *Southern Wine Corp Pty Ltd (in liq) v Frankland River Olive Co Ltd* [2005] WASCA 236; (2005) 31 WAR 162, [30]], and is not subsequently lost by cessation of office, whether by retirement or removal [*Xebec v Enthe*, 898; *Coates v McInerney* (1992) 7 WAR 537; *Southern Wine Corp v Frankland River Olive Co*, [30]; *Dimos v Dikeakos Nominees Pty Ltd* (1996) 68 FCR 39, 43].

20 *Seventhly*, upon bankruptcy or liquidation of a trustee, its right of indemnity vests in its trustee in bankruptcy or liquidator [*Official Assignee of O'Neill v O'Neill* (1898) 16 NZLR 628; *Jennings v Mather* [1901] 1 QB 108, 117; *Savage & Whitelaw v Union Bank of Australasia Ltd* [1906] HCA 37; (1906) 3 CLR 1170, 1188, 1196; *Octavo Investments v Knight*; *Re Suco Gold Pty Ltd (in liq)* (1983) 33 SASR 99, 109; (1983) 7 ACLR 873, 882].

21 *Eighthly*, if the trust property is transferred to a new trustee, the lien survives and the new trustee takes subject to the lien of the old trustee – except perhaps in the exceptional case of a *bona fide* purchaser for value without notice [*Belar Pty Ltd (in liq) v Mahaffey* [1999] QCA 2; [2000] 1 Qd R 477, [20]; *Octavo Investments v Knight*, 370; *Chief Commissioner of Stamp Duties v Buckle*, 246; *Re Exhall Coal Co Ltd* (1866) 55 ER 970].

22 *Ninthly*, a trustee is entitled to retain possession of trust property against a beneficiary until its indemnity is exercised [*Octavo Investments v Knight*, 369-370; *Chief Commissioner of Stamp Duties v Buckle*, 246; *Re Exhall Coal Co Ltd*, 972; *Re Enhill Pty Ltd* [1983] 1 VR 561].

23 At issue in the present case is whether the ninth proposition extends to allow a former trustee to retain assets pending exercise its right of indemnity, not as against a beneficiary, but as against a new trustee. On this issue, the authorities are far from clear.

24 Analysis begins with the judgment of Knight Bruce VC in *Wilson v Parker* (1846) 10 Jur 979, where it was held that a claim by a former trustee for remuneration was no objection to the entitlement of the new trustee to a transfer of the trust assets – though the possibility that a claim for indemnity in respect of expenses incurred might be in a different position was left open.

25 An important case is *Jennings v Mather* [1901] 1 KB 108, a decision of the King's Bench Divisional Court on appeal from the County Court. The Divisional Court upheld the claim of a trustee's trustee-in-bankruptcy over that of the trustee's execution creditor to possession of trust property, on the basis that the trustee's right of indemnity passed to its trustee-in-bankruptcy. Kennedy J said (at 113–4):

It seems to me clear that, on the undisputed facts in the present case, the goods in question come within these decisions, and, so far as common law is concerned, they became as they came in assets of the assignor - that is to say, assets of the trust estate ... if that is so, something follows in equity which, it seems to me, the county court judge has overlooked. While there can be no right of a creditor created in the course of the trading to treat as goods of the trustee goods which form part of the trust estate, still it is equally clear that the trustee has a right and interest in those goods, because he has a right to an indemnity in the nature of a lien over those goods. It necessarily follows, as it seems to me, that the trustee has a right to prevent any person from carrying away those goods, and to say to everybody, including the cestuis que trust, 'I am entitled to an indemnity out of those goods, and have therefore, a pecuniary interest in them.' Of course, when the accounts come to be made up, if it should appear that nothing is due to the trustee on the trading, there is nothing in respect of which he needs to be indemnified, and his lien over the goods is gone; but until the accounts are made up he is entitled to a lien over all the assets of the estate. A lien (putting aside the question of bankruptcy, with which I will deal directly) has always been held to be sufficient title as against the world to hold the goods until that lien is satisfied or is proved not to exist. We are bound, as it seems to me, to enforce the equitable rights of a trustee who, properly and in accordance with his trust, is carrying on a business for the benefit of the trust estate.

26 A number of observations may be made about that judgment. The *first* is, as Mr Ashhurst SC for the applicant points out, allowing the execution creditor to take the property in question would have

destroyed the right of indemnity in respect of it. *Secondly*, the case deals with competing claims to trust assets, between the trustee's execution creditor and the trustee's trustee-in-bankruptcy; it is silent on the position of a replacement trustee. *Thirdly*, the observation of Kennedy J, to the effect that a lien is sufficient title as against the world to withhold goods until the lien is satisfied or proved not to exist, is true of a common law possessory lien, but it is far from clear that it is an accurate statement of a characteristic of an equitable lien.

27 The case went on appeal to the Court of Appeal [*Jennings v Mather* [1902] 1 KB 1]. Stirling LJ said (at 6):

A trustee has for his protection a right to have costs and expenses properly incurred by him in the administration of the trust paid out of the trust property, and the amount of such costs and expenses constitutes a first charge upon that property. A Court of Equity will never take trust property out of the hands of a trustee without seeing that such costs and expenses are reimbursed to him, and that he is relieved from personal liability in respect of them; and, when the legal title to trust property is vested in the trustee, he has a right to resort to that property, without the assistance of the Court, for the purpose of indemnity against liabilities properly incurred by him in the administration of the trust. It is most important that this right should be maintained.

28 Matthews LJ said (at 8-9):

The position originally taken up by the execution creditor left out of sight altogether the right of Mather as a trustee to indemnity out of the trust property, and to hold the goods seized as part of such property until his rights in respect of them are ascertained. That right appears to me clearly to exist, and to form a part of Mather's estate which passed to the claimant as his trustee in bankruptcy. It is impossible at this stage to take an account as between Mather and the trust estate. I think the claimant is entitled to say that such an account cannot be gone into now, but must be taken hereafter in due course, and that, in the meantime, it is sufficient, in order to entitle him to succeed on the interpleader issue as against the execution creditor, who has no title whatever to the goods, that there is primâ facie this equitable lien on the goods in favour of Mather's estate which has passed to him as Mather's trustee in bankruptcy.

29 Again, the observations may be made, *first*, that the context was competing claims by a trustee's execution creditor and trustee-in-bankruptcy, and not by a replacement trustee; and *secondly*, while reference was made to the circumstance that the lien was an equitable one, there does not appear to have been consideration of the characteristics of an equitable lien (and, in particular, that it is not possessory).

30 The next significant case appears to be *Re Pauling's Settlement Trusts (No 2)* [1963] Ch 576; [1963] 1 All ER 857. In that case Wilberforce J (as he then was) held that an order for the appointment of new trustees should not be made, *inter alia* on the ground that the old trustees were entitled to have security for their indemnity, and that to vest the trust fund in new trustees would deprive the old trustees of that security. His Lordship considered the possibility of appointing new trustees and leaving the question of vesting of the assets to be dealt with at a later at a stage, but concluded ([1963] 1 All ER 857, 863): "To appoint new trustees, and at the same time to leave another person not in the position of a trustee in the possession of the trust fund, would be to create a most undesirable situation".

31 With great respect, the suggestion that appointing new trustees and vesting the trust assets in them would deprive the old trustees of security for their indemnity is incorrect. The cases already referred to establish that the security survives and can be enforced against the trust assets in the hands of the new trustees at the suit of the old trustee: see the eighth proposition above (at [21]). Thus, while *Re Pauling's Settlement Trusts (No 2)* suggests that an outgoing trustee is entitled to insist on retaining the trust fund as against the new trustee as security for its indemnity, it appears to overlook the cases that hold that the security survives and is enforceable against the assets in the hands of the new trustee. However, as to the undesirability of a person not in the position of the trustee being in possession of the trust fund, in this case the appointment of a new trustee has already taken place out of Court, so that that position will pertain if the trust fund is not now vested in the new trustee.

32 The next significant case is an Australian one. In *Re Suco Gold Pty Ltd (in liq)* (1983) 33 SASR 99; (1983) 7 ACLR 873, King CJ said (at 109; 882):

The trustee's lien is an equitable lien which confers on him a charge over the trust property, whether in his possession or not, for the purpose of protecting and enforcing the right of indemnity. It also confers on the trustee a right to possession of the trust property for the purpose of protecting and enforcing the right of indemnity, *Jennings v Mather* [1902] 1 KB 2 [sic]. The right of possession of the trustee, until his right of indemnity is exercised, is superior to those of a new trustee or the *cestuis que trust*. The rights conferred by the lien passed to the liquidator. They would enable him to obtain and retain possession of the trust property until the right of indemnity has been exercised, and to realize the trust property in the course of exercising it. The lien is ancillary to the right of indemnity. When the right of indemnity has been exercised by recoupment of any amounts which the trustee has paid in connection with the trust and by payment out of the trust fund of any outstanding liabilities, the lien ceases and the balance of the trust property becomes available to a new trustee or the *cestuis que trust* as the case may be.

33 This is the only case which expressly addresses the position of a new trustee. It is plainly said that the rights of possession of the old trustee prevail over those of the new trustee. However, that observation must have been *obiter*, as no question of a new trustee arose in *Re Suco Gold*; none had been appointed. The only authority cited is *Jennings v Mather*, which I have already discussed above.

34 The High Court of Australia touched on the issue in *Octavo Investments v Knight*, where in the joint judgment of Stephen, Mason, Aitkin and Wilson JJ it was said (at 369-70):

Property which is an asset of a trading estate carried on by a trustee is properly described as trust property: *Dowse v. Gorton* [1891] AC 190; *Jennings v. Mather* [1901] 1 QB, at p 111 . However, as we have already indicated, that does not mean that the cestuis que trust are necessarily entitled to call for the delivery of the property. If the trustee has incurred liabilities in the performance of the trust then he is entitled to be indemnified against those liabilities out of the trust property and for that purpose he is entitled to retain possession of the property as against the beneficiaries. The trustee's interest in the trust property amounts to a proprietary interest, and is sufficient to render the bald description of the property as "trust property" inadequate.

35 This passage establishes that the trustee is entitled to retain possession of trust property as against the beneficiaries in aid of the trustee's right of indemnity. It says nothing in respect of the

position as against a replacement trustee. As Mr Ashhurst pointed out, distribution to the beneficiaries would at least arguably be destructive of the security interest. In any event, retention by the trustee as against the beneficiary is consistent with equitable concepts of set-off, and the rule that a trustee is not required to make a distribution to a beneficiary to the extent that the beneficiary has outstanding obligations to the trust, to which I shall return. Unlike distribution to a beneficiary, transfer to a new trustee of the trust assets is not destructive of the old trustee's lien [see *Fletcher v Collis* [1905] 2 Ch 24, 35 (Romer LJ); *Re Pauling's Settlement*, 585; 861].

36 To this point, then, the position appears to be that one case – *Re Suco Gold*, a decision of the Full Court of the Supreme Court of South Australia – specifically asserts that the trustee's right to possession takes priority over the entitlement of replacement trustee, but that is apparently *obiter*. There are two cases – *Octavo Investments v Knight*, in the High Court of Australia, and *Jennings v Mather* – which suggest that the equitable lien of a trustee is possessory at least to the extent that it entitles the trustee to retain possession as against (in the one case) a beneficiary, and (in the other) an execution creditor; but those cases otherwise say nothing as to the position as against a successor trustee.

37 However, there are then a number of local authorities. In *Global Funds Management (NSW) Ltd v Burns Philp Trustee Co Ltd (in prov liq)* (1990) 3 ACSR 183, Rolfe J, founding on a passage in *Jacobs' Law of Trusts in Australia*, 5th ed, held that the trustee's lien could, in certain circumstances, be suspended and the trust assets transferred to a new trustee, subject to appropriate orders or undertakings protecting the lien. His Honour said (at 186):

The suggestion that Burns Philp holds a lien over the trust assets to enable it to enforce its indemnity so that the appointment of a new trustee would be somewhat academic because no assets would be vested in him is not, in my opinion, a valid ground for refusing to appoint a new trustee. I do not understand the submission to which I have just referred to have been made on the basis that Burns Philp would refuse to comply with any vesting order made by the court per se, but rather that Burns Philp would assert its entitlement to a lien over the trust assets until such time as its entitlement to an indemnity from the trust assets has been determined. In my opinion the vesting of the property of the trusts in a new trustee would not bring about the result that Burns Philp would lose its right to an indemnity. The position of Burns Philp to assert an indemnity against the trust assets can be protected by the making of an appropriate order or the proffering of appropriate undertakings, which would ensure that the trust assets are not diminished, other than in carrying on the ordinary business of the trust, or that the trusts' liabilities are not increased save in the same way. There is no real doubt that the lien, in certain circumstances may be suspended. One such circumstance, which arises in the present case, is whether Burns Philp has a right to an indemnity. I appreciate that Burns Philp asserts it has not lost that right but the authors of *Jacobs Law of Trusts in Australia* (5th ed) at para 2104 state: "Hence, if there is *any doubt* about the matter, both his indemnity and the lien protecting it may be suspended pending investigation of his accounts." (My emphasis).
On the facts before me, and I refrain from saying more about it because it will be the subject of other litigation, I am satisfied that there is at least a doubt. I consider, therefore, that subject to an appropriate safeguard of the type to which I have referred, this is a proper case for the suspension of the lien.

38 In *Hillig v Darkinjung Local Aboriginal Land Council* [2006] NSWSC 1371, Barrett J declined to make a vesting order in the absolute terms sought, on the grounds that to do so would deny the "preferred beneficial interest" of a trustee in the relevant property. His Honour said (at [17]-[18]):

[17] The third point goes to the matter raised by DPL concerning preservation of the trustee's indemnity. Particularly where a winding up application is pending and seems most likely to produce an administration in insolvency, I am not satisfied that it is sufficient to look at that matter simply in terms of set-off. A trustee's right to be indemnified out of trust assets is given effect to by means of an equitable interest in the whole of the assets of the trust. Until the right to be indemnified is exercised, the trustee has a right to possession superior to the rights of the beneficiaries (*Re Suco Gold Pty Ltd* (1983) 33 SASR 99 at p.109 per King CJ) and a "preferred beneficial interest in the trust fund" (a description applied by Sheller JA in *Chief Commissioner of Stamp Duties v Buckle* (1995) 38 NSWLR 574 at p.586 and expressly approved by the High Court in *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4; (1998) 192 CLR 226 at p.247). Until satisfaction of the trustee's right of indemnity, it is not possible to say what the trust fund is: *CPT Custodian Pty Ltd v Commissioner of State Revenue* [2005] HCA 53; (2005) 79 ALJR 1724 at [51].
[18] If the court were to make a vesting order in the terms sought by DLALC, the "preferred beneficial interest" of DPL in the property concerned would be denied. The "preferred beneficial interest" might be of particular significance in an insolvent administration of DPL, particularly if the right of DLALC in respect of unpaid equitable compensation was no more than a debt provable along with all others. It may be that a vesting order could be framed in a way that excepted or reserved the interest of the trustee (see, for example, *Global Funds Management (NSW) Ltd v Burns Philp Trustee Co Ltd* (1990) 3 ACSR 183 at p.186), but the efficacy of such a course in respect of the *Real Property Act* land could present problems, having regard to s.86 of that Act.

39 However, his Honour then proceeded to conclude that the appropriate course was to require the old trustee to transfer all the trust assets to the new trustee except for a specified sum which was to be paid into Court pending resolution of the old trustee's claim to indemnity and upon resolution and satisfaction of those claims then to the new trustee. In other words, sufficient was to be retained from the trust assets to cover the old trustee's claim, and the balance transferred to the new trustee. This is consistent with *Kemtron Industries Pty Ltd v Commissioner of Stamp Duties* [1984] 1 Qd R 576, in which McPherson J held that the trustee's right of retainer extended only to sufficient assets to cover the trustee's claim for indemnity, and did not entitle the trustee to retain all the assets in satisfaction of a claim which would easily be satisfied out of only a small proportion of them (at 587).

40 Those cases are significant because they tell against the notion that the trustee's equitable lien – which on the authorities plainly extends to all the trust assets – gives the trustee a right to possession of all of those assets. If it gave a right to possession of all of the assets to which it attached, then –contrary to *Kemtron Industries v Commissioner of Stamp Duties* and *Hillig v Darkinjung Local Aboriginal Land Council* – the trustee would be entitled to retain the whole, and not only a portion, pending the resolution of its claim to indemnity.

41 Then, in *Ronori Pty Ltd v ACN 101 071 998 Pty Ltd* [2008] NSWSC 246, Barrett J returned to the same issue. His Honour said (at [15]-[18]):

[15] In the present case, therefore, the former trustee continues to enjoy a beneficial interest in the trust property commensurate with its right of indemnity out of that property. Although the trustee's right to resort to trust property is sometimes described as a lien, it is not essential for the enjoyment and effectuation of the right that possession of the trust property be retained. The right entails, as I have said, a beneficial interest in the property. It is not in the nature of a possessory security.
[16] Where there is a change of trustee, the former trustee's interest remains enforceable against the trust property. It is relevant, in this connection, to quote a passage from the joint judgment of

Thomas JA, Shepherdson J and Jones J in *Belar Pty Ltd v Mahaffey* [1999] QCA 2; [2000] 1 QdR 477 (at [19] to [21]):
“In conducting the business of the trust, the trustee becomes personally liable for debts incurred.

‘However, he is entitled to be indemnified against those liabilities from the trust assets held by him and for the purpose of enforcing the indemnity the trustee possesses a charge or right of lien over those assets.’ [*Octavo Investments Pty Ltd v Knight* [1979] HCA 61; (1979) 144 CLR 360 at 367]

That is a reference to trust assets in the trustee’s possession. When there is a change of trustee with the trust assets being vested in the new trustee, the former trustee no longer has direct access to such assets, and should make the necessary claim for indemnity against the trustee who represents the trust.
The trustee’s right of indemnity out of the trust assets is in the nature of a charge or lien in favour of the trustee and as such takes preference or priority over claims by the cestuis que trust. But of course when the assets have passed out of a trustee’s possession the necessary claim for a trustee’s indemnity should be made against the new trustee. An unco-operative new trustee who declined to exercise the powers to recover trust property in the hands of the beneficiaries could be made a defendant, and orders could be made which would in effect permit the former trustee to exercise such powers by subrogation.
There is ultimately a right to proceed directly against the beneficiaries but that right depends upon exhaustion of any remedy against the personal representative.”
[17] This passage was expressly approved by Spigelman CJ in *Gatsios Holdings Pty Ltd v Nick Kritharas Holdings Pty Ltd* (2002) ATPR 41-864; [2002] NSWCA 29 at [2].
[18] It is thus clear that, even though the trust assets have passed out of the former trustee's possession, the vindication of that person’s beneficial interest remains available by way of an appropriately constituted claim against the new trustee. There need therefore be no concern on the part of the court about recognising immediately the right of the new trustee to have the trust property vested in it.

42 His Honour therefore made a declaration that the plaintiff was the trustee in succession to and substitution for the defendant and stood the proceedings over, in the expectation that the defendant would, in accordance with a provision in the Trust Deed which obliged it to take such action necessary to vest the new fund in any Trust Deed in recognition of the declaration made.

43 In earlier editions of Underhill and Hayton's *Law of Trusts and Trustees*, the authors expressed doubt as to whether a trustee, having a charge or equitable lien, could refuse to transfer the property to new trustees until the charge was satisfied. However, in the 16th edition it is said (at 819-20), "A trustee can refuse to transfer property to new trustees or absolutely entitled beneficiaries until his lien is satisfied". The only authority cited for this proposition is *X v A and Others* [2000] 1 All ER 490, which, on examination, while considering the nature of a trustee's lien, says nothing as to the rights of the trustee in these circumstances against a successor trustee.

44 As I have said, that leaves the authorities in a state of some disarray. Ordinarily, a judge sitting at first instance would give considerable deference to a judgment of the Full Court of another State, where there was no binding local authority. However, the force of that is reduced to some extent in this case, *first*, by the circumstance that, as I have said, the relevant observations in *Re Suco Gold* appear to be *obiter*; and, *secondly*, by the existence of local authority to which, though first instance decisions and thus not strictly binding on me, and though they have not considered *Re Suco Gold*, nonetheless I would ordinarily out of comity afford due deference.

45 Ultimately, I think it is preferable I seek to resolve this issue as a question of principle, rather than by trying to reconcile what appear to be conflicting authorities, none of which are strictly binding.

46 The starting point is that it is universally accepted that the nature of the trustee's interest is that of an equitable lien – that is, an equitable security interest arising not by agreement of the parties but by operation of law. It is also universally accepted that the only remedy of the trustee against the trust assets is judicial sale or appointment of a receiver. That is consistent with the nature of an equitable lien as a mere hypothecation. Such a security does not confer on the security holder any right of foreclosure, nor any right to possession of the property. It creates an interest which the security holder can enforce, as I have said, by judicial sale or appointment of a receiver, but such a security holder cannot bring an action for possession of the property the subject of the equitable lien. It seems to me to follow that, insofar as *Jennings v Mather* – which in turn influenced the observations in *Re Suco Gold* – depends on the view that the trustee's lien carries with it a right to retain possession, it is mistaken.

47 But it is necessary to consider whether the view that an equitable lien does not confer a right to possession of the subject property can be reconciled with those cases which establish that the trustee is entitled to retain trust property as against a beneficiary or an execution creditor. At least as against a beneficiary, the answer is that that entitlement is a manifestation of set-off, in that once a trustee has an accrued right of indemnity, the trustee is entitled to set it off against the beneficiary's claim to the trust assets, and to refrain from distributing until the trustee's claim is satisfied. In the closely analogous field of the trustee's personal right of indemnity against a beneficiary, this was explained in *Re Akerman* [1891] 3 Ch 212 by Kekewich J (at 219):

A person who owes an estate money, that is to say, who is bound to increase the general mass of the estate by a contribution of his own, cannot claim an aliquot share given to him out of that mass without first making the contribution which completes it. Nothing is in truth retained by the representative of the estate; nothing is in strict language set off; but the contributor is paid by holding in his own hand a part of the mass, which, if the mass were completed, he would receive back.

48 As the authors of *Jacobs' Law of Trusts*, 5th ed, point out (at [2111]): "The beneficiary is treated as already having in his hands a portion of the assets and therefore is satisfied *pro tanto*". This is also reflected in the cases to which I have referred such as *Hillig v Darkinjung Local Aboriginal Land Council*, *Jennings v Mather* and *Kentrom Industries v Commissioner of Stamp Duties*, which establish that the trustee is entitled to retain only sufficient to cover the indemnity and not more.

49 A second explanation – which applies both to distribution as to beneficiaries, and to execution creditors as in *Jennings v Mather* – is that a distribution to a beneficiary or seizure by an execution creditor would be destructive of the security interest, whereas transfer to a new trustee is not.

50 To my mind, then, it follows in principle that a former trustee does not have a right to retain, as against a new trustee, the trust assets as security for an accrued right of indemnity, though the former trustee is entitled to ensure the new trustee does not take steps which will destroy, diminish or jeopardise the old trustee's right of security, which subsists in the trust assets after their transfer to the new trustee. This view accords with the conclusions of Rolfe J and Barrett J in the New South Wales cases to which I have referred. It follows that I respectfully decline to follow the

observations of the Full Court of Supreme Court of South Australia in *Re Suco Gold*.

51 As in *Ronori v ACN 101 071 998*, clause 27.1 of the Trust Deed in the instant case, which I have set out above, reinforces this conclusion.

52 (NSW) *Trustee Act* 1925, s 9, relevantly provides as follows:

(1) Where a new trustee is appointed, the execution and registration of the deed of appointment shall without any conveyance, except as otherwise provided in this section, vest in the persons who become and are the trustees for performing the trust, as joint tenants and for the purposes of the trust, the trust property for which the new trustee is appointed.
...
(3) In the case of land subject to the provisions of the Real Property Act 1900, the property shall not vest until either:

(a) the appropriate transfer is executed and registered, so that the property is duly transferred, or

(b) an entry of the vesting is made by the Registrar-General.

Any such entry shall have the same effect as if the property were duly transferred.
...
(4) In the following cases the property shall not vest until the appropriate transfer is executed and registered so that the property is duly transferred, that is to say, in the case of:

(a) any property comprised in a mortgage for securing money subject to the trust, where the property is not either land subject to the provisions of the Real Property Act 1900 or land conveyed on trust for securing debentures or debenture stock,

(b) (Repealed)

(c) any property a conveyance of which is required to be registered by or under any Act, whether of this State or otherwise, other than the Acts mentioned in subsections (3) and (3A).

...
(7) If any property does not vest under this section until transfer or registration, the execution and registration of the deed of appointment, or of the deed or deeds of consent and retirement, as the case may be, shall nevertheless vest the right to call for a transfer of the property, and to sue for or recover the property.
...

53 The effect of s 9 is that trust assets, other than those specifically exempted, vest upon execution and registration of the Deed of Appointment without need for any conveyance. The Deed of Appointment was registered on 4 November 2008. Accordingly, that was effective to vest all assets other than those specifically excluded by s 9 in the new trustee, without any necessity for a vesting order. In respect of the remaining assets, including interests in (NSW) *Real Property Act* 1900 land, sub-section 7 gives the new trustee the right to call for a transfer, and to sue for or recover the property. A vesting order is an extraordinary remedy, not intended to replace ordinary conveyancing or transfer mechanisms [*Hillig v Darkinjung Local Aboriginal Land Council*, [16]; see also the course adopted by Barrett J in *Ronori v ACN 101 071 998*].

54 The position to this point can thus be summarised as follows. *First*, the loans and the securities and the causes of action arising from them in the third party proceedings are trust assets of the Reliance Discretionary Trust. *Secondly*, RFSNSW has been appointed new trustee of that trust in place of Reliance. *Thirdly*, the old trustee Reliance has no right to retain those trust assets as against the new trustee. *Fourthly*, the assets other than those specifically exempted by s 9 have already vested in the new trustee by operation of s 9, and the new trustee is entitled to call for transfers of those which have not already vested. *Fifthly*, the causes of action having vested in the new trustee, Reliance no longer has any title or standing to maintain them; only the new trustee RFSNSW has. *Sixthly*, the new trustee should, therefore, be substituted for Reliance as the relevant party in each of those proceedings.

55 These conclusions are, in my view, based on right rather than on discretion. Argument was raised as to various discretionary considerations which, ultimately, I think are not relevant. However, lest I be wrong in that respect and lest it be appropriate to consider discretionary questions, the considerations are these. *First*, despite arguments advanced by the liquidator and on behalf of Ms Zeaiter and Mrs Mizzi, I did not see how any prejudice could be occasioned to the third parties from the substitution of the new trustee for the old. Insofar as I have concluded that the proceedings were brought on behalf of the trust by Reliance acting as trustee, then its right of indemnity will be preserved against the trust assets in the hands of the new trustee. An undertaking is proffered by RFSNSW not to compromise the causes of action, and to pay any proceeds into a controlled moneys account. It seems to me that there is simply no jeopardy involved to the former trustee's right of indemnity nor to any rights of the third parties. On the other hand, insofar as the beneficiaries of Reliance Discretionary Trust are concerned, both in terms of being funded to prosecute the proceedings, and in terms of having the requisite knowledge of the underlying events and background, RFSNSW is in a vastly superior position to the liquidator properly to prosecute the proceedings.

Orders

56 My orders are:

(1) Pursuant to (CTH) *Corporations Act* 2001, s 471B, grant leave insofar as it be required to Reliance Financial Services NSW Pty Ltd to institute and continue the proceedings contained in its interlocutory process filed 25 July 2008 against the first respondent Reliance Financial Services Pty Ltd (in liq).

(2) Declare that the applicant Reliance Financial Services NSW Pty Ltd was appointed trustee of the Reliance Discretionary Trust in place of the first respondent Reliance Financial Services Pty Ltd on 26 June 2008.

(3) Declare that the loans the subject of the following proceedings are, or in the case of Mrs Mizzi, were, assets of the Reliance Discretionary Trust:

(a) Reliance Financial Services Pty Ltd v Annette Theresa Zeaiter (Matter No 3801/06);

(b) Reliance Financial Services Pty Ltd v Josephine Mizzi (Matter No 2818/05);

(c) Reliance Financial Services Pty Ltd v Marthas T Market Pty Ltd (Matter No 4065/03);

(d) Reliance Financial Services Pty Ltd v Criniti, Castellano & Romano (Matter No 1832/05);

(e) Reliance Financial Services Pty Ltd v Griffith & CKM (Mortgages) Ltd (Matter No 3465/07);

(f) Reliance Financial Services Pty Ltd v Sobbi & Sobbi (Matter No 12224/04);

(g) Reliance Financial Services Pty Ltd v La Hood (Matter No 15776/07).

57 The next appropriate step, in each of the proceedings other than the Mizzi proceedings, would be an order substituting RFSNSW for Reliance. Those proceedings are not all presently before the Court, but given the relief sought in the interlocutory process that may not be an obstacle; I will hear the parties on this shortly.

58 So far as the proceedings concerning Mrs Mizzi are concerned, the logical consequence of the conclusions to which I have come are that RFSNSW should be substituted as appellant in the proceedings in the Court of Appeal. It may be that in the light of this judgment that can now be done consensually, but otherwise it would be necessary for an application to that effect to be made to the Court of Appeal.

59 I do not propose to make a vesting order, as it seems to me that there is no reason to suspect that insofar as any further action is required, the entitlement to possession now having been established, the liquidator will not do what is required to vest the trust assets in the new trustee. If there is any difficulty in that respect, the matter may be dealt with on a subsequent occasion.

60 The necessary consequence of the conclusions I have reached is RFSNSW is entitled to be substituted for Reliance in each of the third party proceedings to which I have referred. Some of those proceedings are in this Division, others are in the Common Law Division, and one is in the Court of Appeal. The appropriate course is that, having given that indication and made the other orders which I have mentioned, I should adjourn these proceedings to the date to which I have adjourned the Dayroll proceedings and direct that the other matters – those of them that are in the Common Law Division, subject to obtaining the approval of the Chief Judge of Common Law – be listed before me on that date, when they can all be addressed.

61 I will, therefore, adjourn the proceedings to Monday, 24 November 2008, at 9.30am.

62 I direct that each of those proceedings 3801/06, 2818/05, 4065/03, 1832/05, 3465/07, 12224/04 and 15776/07 be listed before me on that date.

63 I direct that the present applicant RFSNSW notify all parties in each of those proceedings of the date, time and place of that appointment for hearing and of the substance of the orders made today and of the proposal that on 24 November an order would be made in each proceeding substituting RFSNSW for Reliance, and, as soon as it becomes available, provide a copy of these reasons for judgment.

Costs

64 The applicant has succeeded, albeit not on every ground nor for all the relief originally sought in the interlocutory process. However, it has not been established that any additional costs were incurred by reason of that part of the interlocutory process which was not pressed.

65 The cases to which I have referred in the substantive judgment show that upon a trustee

becoming bankrupt or going into liquidation, the trustee-in-bankruptcy or liquidator succeeds to the trustee's right of indemnity and equitable lien. In those circumstances, I agree with Mr Allen’s submission that Mr Donnelly in his capacity as liquidator of Reliance was an appropriate party to the application.

66 Mrs Zeaiter could have submitted to the relief sought, but chose to oppose it and to support the position of the liquidator, and did so not only on the grounds advanced by the liquidator but on additional grounds set out in her own written submissions. Having entered into the fray in that way, it is not open to her to say that just because costs would have been incurred by the liquidator's opposition in any event, she should for some reason be exempted from liability for costs.

67 Similarly, Mrs Mizzi joined in the liquidator's opposition to the proceedings and advanced her own submissions, including that it was not established that the relevant loans were trust assets. While I have not in these proceedings made a formal order substituting RFSNSW in the appeal in the Mizzi proceedings, I have declared that the Mizzi loan was an asset of the trust, a position which Mrs Mizzi opposed.

68 I order that the second, third and fourth respondents pay the applicant's costs of interlocutory process filed 25 July 2008. I adjourn the proceedings to 9.30am on Monday, 24 November 2008, before me.

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