Bucolic Dream or Arboreal Fantasy? The Willmott Saga, Insolvency Disclaimers and the Contract/Property Dichotomy

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Introduction

An option is often provided in insolvency legislation to disclaim property belonging to a debtor whose maintenance within the estate is deemed to constitute a liability. While by no means a generalised rule, enough jurisdictions have adopted this rule that it is recognised in the UNCITRAL Legislative Guide to Insolvency Law 2004 as forming one of the many recommendations for adoption by all insolvency regimes. A typical disclaimer provision normally allows an insolvency practitioner administering the estate to disclaim an on-going obligation in circumstances where requiring the debtor to remain bound by a contract would constitute an impediment to the efficient administration and conclusion of proceedings involving that debtor. Other property may be disclaimed where its maintenance may be unprofitable and result in further obligations or burdens being acquired, which ultimately are of little or no value to the estate. Justification for disclaimers sometimes refers to the harm to the general mass of creditors if maintenance of the property further diminished the pool available for distribution. As such, general creditors may not be said to have bargained for such burdens or obligations and fairness principles would require exclusion of the asset from the estate, reverting to the former owner or holder of a superior interest. Cases have, however, highlighted the particular problem of environmental obligations in relation to disclaimed property, especially if the disclaimer results in the public purse having to bear the cost.

In a number of jurisdictions, seeking the permission of the court is a necessary pre-condition to exercising the power. Notice to affected parties

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may also be a requirement, permitting usually limited challenges to the proposed divestiture. There may also be a specified timeframe for the disclaimer to take effect and determining the extent of any unexpired obligation, thus binding parties as well as any third parties with claims derived from original title-holders. Nonetheless, affected parties do not remain wholly without remedy, as they may (usually) prove as unsecured creditors, albeit the chances of a distribution are slim. Alternatively, some jurisdictions authorise the same parties to apply for vesting of the property in them, especially if they have rights dependent on the debtor’s, for example sub-leases and like interests. Overall, the intention behind the disclaimer provisions is that to shed such property from the estate to allow for easier and faster administration of the insolvency.

This article intends firstly to explore the history of the disclaimer option as it has been received into Australian legislation, giving some examples of past use. Then, in light of recent case-law, particularly the Willmott case discussed below, this article will question whether the courts have interpreted correctly the purpose and remit of the section in determining this case. The article will also go on to consider whether the trend for the contractualisation of “commercial” leases in the case is correct, given the judges’ reasoning, and whether there are any natural limits to the extension of the doctrine. The article will also canvass what limitations there may be on the use or impact of the disclaimer provisions, particularly any problems raised by their potential extension in circumstances not originally foreseen in the insolvency context. Lastly, the article will outline whether there is any case for reform of either the statutory provision or of the contractualisation trend.

The Australian Disclaimer Provisions

The transmission of English bankruptcy models, in particular the 1869, 1883 and 1914 legislation, to various territories within the then British Empire (now Commonwealth) saw similar statutes being enacted elsewhere. This also led to a generalised acceptance of the place of the disclaimer provision that had first appeared in bankruptcy legislation in 1869, when it was adopted in England and Wales to replace the doctrine of election that bound a trustee to perform contracts or retain property within the estate subject to any burdens. Once the disclaimer provision began appearing within companies’ legislation, they were transmitted along with the models extended or adopted elsewhere, especially those in the Companies Acts of 1929 and 1948. As part of this process, the disclaimer provision in Australia first appeared in State bankruptcy legislation in the late 19th and early 20th centuries. When the Federal Government became responsible for regulation of personal

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5 See *Enron Australia v TXU Electricity* [2003] NSWSC 1169, at paragraphs 62-65 for a brief history of the provision following its adoption as section 23, Bankruptcy Act 1869.
7 Examples of related provisions include Articles 171-173, Companies (Jersey) Law 1991; section 296, Companies Act 1965 (Cap. 125) (Malaysia); section 332, Companies Act 1967 (Cap. 50) (Singapore).
insolvency, it was enacted as section 14 of the Bankruptcy Act 1924, closely modelled after the English provision. The reshaping in light of the work of the Clyne Committee between 1956 and 1962, leading to the passing of the Bankruptcy Act 1966, cast the provision in a form that would be very familiar today. Changes resulting from the Bankruptcy Amendment Bill 1979 extended the provision to enable the disclaimer of any contract, including those in relation to unsaleable, though not unprofitable, property. It also required notice to interested parties of the intention to disclaim any lease. Reviewing the shape of insolvency law in Australia, the Harmer Report made recommendations for the harmonisation of the disclaimer provisions across corporate and personal insolvency law. Chapter 13 on “Insolvency Administration” of the Harmer Report made the point that, though infrequently used, the disclaimer is an important tool to avoid the possibility of the office-holder’s personal liability for contracts. Having analysed the previous law and the differences between personal and corporate insolvency provisions, the Harmer Report’s recommendations centred on expanding the power to disclaim in corporate insolvency and recasting the definition of disclaimable property. It also suggested that there should be no difference between the disclaimer of a lease and other onerous property. Further recommendations included removing time limits on disclaimers and providing for notice of a disclaimer to affected parties, who would be able to challenge its effects. Ultimately, the Harmer Report led to the introduction of what is now section 568 of the Corporations Act 2001, a provision more or less in keeping with its recommendations.

The present legislative framework for disclaimers, set out in Division 7A of the Corporations Act 2001, contains one of the most complex sets of provisions amongst common law countries. According to the law, a disclaimer may be made at any time in writing and signed on behalf of the company by a liquidator. Property is defined widely to include land burdened with onerous covenants, shares, unsaleable or not readily saleable property, property

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8 The Cork Report, at paragraph 1193, also referred to the Clyne Committee’s recommendations for a general power to disclaim that appeared in section 133, Bankruptcy Act 1966.
10 See Cork Report, at paragraph 1191, making the same observation, attributing it to the provisions’ complexity and compliance costs, encouraging private resolution by the parties through surrender, assignment or abandonment.
11 Harmer Report, at paragraph 611.
12 Ibid., at paragraph 613. The power to disclaim would also be provided to an administrator (at the creditors’ behest), but not to a receiver (at paragraphs 621-622).
13 Ibid. at paragraph 614.
14 Ibid., at paragraph 620.
15 Ibid., at paragraph 616.
16 Ibid., at paragraph 618. Failure to challenge or a failed challenge would backdate the effectiveness of the disclaimer to the moment notice was given.
19 Onerous covenants mean not just covenants in the traditional sense, but also other obligations that weigh on the land, for example mortgages and rates. See J. Duns, Insolvency
giving rise to a liability to an onerous obligation or a requirement to pay money, property whose realisation costs (including charges and expenses) would exceed, in all reasonable expectation, the proceeds of sale as well as any contract. 20 The facility to disclaim is available for all types of property (excepting contracts) irrespective of whether the liquidator has tried to sell the property, has taken possession of it or has exercised an act of ownership over the property. 21 As far as contracts are concerned, the facility remains available even though the liquidator may have exercised rights or attempted to assign the contract or any property it covers. 22

As an exception to the general rule that the liquidator is not required to seek the leave of the court, all disclaimers of contract, with two exceptions, relating to unprofitable contracts and leases of land, can only be made with leave being sought. 23 Leave will generally be granted by the court subject to conditions and the making of any orders the court considers just and equitable. 24 Loss of the right to disclaim may occur where a person with a property interest makes an application in writing to the liquidator for the determination of a decision in relation to property or a contract. 25 In this case, the liquidator has a period of 28 days (subject to possible extension) to disclaim, in default of which disclaimer is unavailable and, in the case of a contract, the liquidator is taken to have adopted it. 26 In relation to contracts, the court also has the power, on application of an interested person, to either discharge the contracts on terms as to payment by one or other party of damages for non-performance to the other as the court thinks proper or the rescission of the contract followed by restitution of property. 27 Any sums payable by virtue of an order the court makes may be proved in the insolvency. 28

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20 Section 568(1)(a)-(f), Corporations Law 2001.
21 Ibid., section 568(1)(g).
22 Ibid., section 568(1)(h). Section 568(1AA) disapplies this provision to share buy-backs and retention of title under the Personal Property Securities Act 2009.
23 Ibid., section 568(1A). Keay and Murray, op. cit., at 339, point to the definition of what may be unprofitable contracts, citing Transmetro Corporation Ltd v Real Investments Pty Ltd (1999) 17 ACLC 1314 and Global Television Pty Ltd v Sportvision Australia Pty Ltd (2000) 35 ACSR 484. Duns, op. cit., at 239, suggests that "unprofitable" could also include a substantial financial outlay necessary to continuing performance, citing Dekala Pty Ltd (in liq) v Perth Land and Leisure Ltd (1989) 17 NSWLR 664. Nonetheless, also citing Transmetro, Duns suggests that comparative financial advantage from a disclaimer, where the liquidator could continue to perform the contract without prejudicing his duty to realise assets for the benefit of creditors, would not be sufficient reason to authorise the disclaimer.
24 Ibid., section 568(1B).
25 Ibid., section 568(8)(a). Duns, op. cit., at 237, suggests that a property interest necessarily means a legal or equitable interest and would thus exclude a mortgagee of Torrens title land as well as the holder of a lien, citing the authority of Re Williams; Ex parte Perpetual Trustees, Executors and Agency Co of Tasmania (1931) 26 Tas LR 82 and Re Hensbergen and Aikman; Ex parte Cleland (1950) 15 ABC 238.
26 Ibid., section 568(8)(b).
27 Ibid., section 568(9).
28 Ibid., section 568(10).
Notice requirements are a strong feature of this framework. As part of the disclaimer process, the liquidator may notify a person requiring the making of a statement of interest in relation to property for the purposes of determining whether the property is onerous. Compliance within 14 days is required.\(^{29}\) Notice of the disclaimer itself is also required. Once property has been disclaimed, the liquidator must also give notice to interested parties and to the Australian Securities and Investments Commission, which may also be provided to any person having or claiming to have an interest in property.\(^{30}\) Notice must also be given to a regulatory authority whose function is to note or register property transfers under federal and/or state laws.\(^{31}\) Where the liquidator has cause to suspect that some third party may have an interest, but they are not immediately locatable, the liquidator must advertise the proposal in a newspaper circulating in the state or territory where either the property is situated or the company has carried on business in the 6 months preceding the opening of proceedings.\(^{32}\)

The function of notice generally is to permit challenges by interested parties to disclaimers, which may take place either before or after the disclaimer takes effect. In the case of prior challenges, the law provides that an applicant claiming an interest must apply within 14 days of receipt of personal notice from the liquidator or, where publication in a newspaper has occurred, within 14 days from publication. The same grace period also applies where the liquidator has lodged notice with one of the regulatory authorities.\(^{33}\) On application, the court may set aside the disclaimer and/or make such further order as it thinks appropriate.\(^{34}\) The court must not, however, make an order unless it is satisfied that the claimant would suffer prejudice that is grossly disproportionate when compared to the prejudice that would result to the company’s creditors by setting aside the disclaimer.\(^{35}\)

In the case of post-event challenges, an applicant must apply for leave to set aside the disclaimer,\(^{36}\) which will only be granted if the court is satisfied it would not have been reasonable for the applicant to have taken steps prior to the disclaimer becoming effective.\(^{37}\) Again, in this situation, a court may set aside the disclaimer, but may also make a further appropriate order to restore the company, the liquidator or any other person in the position they would have been in had the disclaimer not taken effect.\(^{38}\) However, there is a presumption against the making of such an order with the court having to be satisfied not only that the prejudice to the applicant is grossly disproportionate to that caused to the company’s creditors by reversing the effect of the

\(^{29}\) Ibid., section 568(13).
\(^{30}\) Ibid., section 568A(1)-(b).
\(^{31}\) Ibid., section 568A(1)(d).
\(^{32}\) Ibid., section 568A(1)(c), applying the publication requirements in section 568A(2).
\(^{33}\) Ibid., section 568B(1).
\(^{34}\) Ibid., section 568B(2).
\(^{35}\) Ibid., section 568B(3).
\(^{36}\) Ibid., section 568E(1).
\(^{37}\) Ibid., section 568E(2)-(3).
\(^{38}\) Ibid., section 568E(4).
disclaimer, but must also consider the interests of other parties who may have relied on the disclaimer taking effect.  

Where a disclaimer is not challenged or no challenge is successful, a disclaimer is taken to terminate the company’s rights, interests and liabilities in the property concerned, but has no effect on any other person, except insofar as necessary to give effect to the release to the company. Any person who suffers a loss as a result of the disclaimer having effect may prove the debt. The date on which the disclaimer is deemed to take effect is when the application to set aside is unsuccessful or the period for challenge expires without an application. In these cases, the date of effect is backdated to the day after the expiry of the notice periods the liquidator is required to comply with. Only where an application is successful is the disclaimer deemed not to have had any effect. Determining the effect of a disclaimer may be problematic. Duns cites the example of Re Tulloch, in which the sole asset was land subject to a mortgage in excess of its value, which the liquidator wished to disclaim after an unsuccessful receivership and attempt to sell the property. Regulatory authorities owed land tax and rates desired a compulsory sale in which their claims would trump the mortgagee’s or, as an alternative, that the land vest in the mortgagee, an order that was resisted. The mortgagee also resisted the disclaimer, the effect of which would have been to vest the property in the Crown with the claimants losing their rights. The court was not prepared to override the mortgagee’s objections to vesting and also considered the effect of the property vesting in the Crown, accordingly, refusing the disclaimer.

As an alternative to simple disclaimer, the court may make an order vesting the property in or delivering it to a third party, where that person is entitled to the property or where the court deems delivery appropriate to that person as well as any trustee for entitled or appropriate persons. The court may do so on the application of a person claiming an interest or subject to an obligation in respect of property and after hearing any person it deems appropriate. The effect of the vesting order is generally to transfer property without any subsequent conveyance, transfer or assignment being required, although

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39 Ibid., section 568E(5). A successful argument did arise in In the matter of Argyle Gravel & Concrete Pty Limited [2013] NSWSC 374.
40 Ibid., section 568D(1). Keay and Murray, op. cit., at 340, cite Sandtara Pty Ltd v Abigroup Ltd (1996) 19 ACSR 578, asserting that covenants in a disclaimed lease are not themselves determined and a guarantor will remain liable, albeit with a provable debt.
41 Ibid., section 568D(2). Duns, op. cit., at 241, cite Re Richardsons Meat Industries Ltd (1989) 15 ACLR 343 as authority for the creditor whose lease contract was disclaimed to prove future rent less an amount for acceleration.
42 Ibid., section 568C(1).
43 Ibid., section 568C(3).
44 Ibid., section 568C(2).
45 Re Tulloch Ltd (in liq) and the Companies Act (1978) 3 ACLR 808.
48 Ibid., section 568F(2).
49 Ibid., section 568F(3).
state and Commonwealth statutes may still impose an obligation to effect registration, pending which the property transfer has only effect in equity.\(^{50}\)

The Willmott Saga

The *Willmott* case arose from the failure of a company engaged in the agri-business sector in 2010. A number of large plantation businesses of a similar type had also failed in the years preceding this, including Environinvest, Forestry Enterprises Australia, Great Southern and Timbercorp. What the companies sold, via managed investment schemes, was the opportunity to invest in the agricultural and/or forestry sectors and to realise over time profits from the sale of crops and forestry products. The market was focused in particular on softwoods, for which demand would undoubtedly be forthcoming, given high prices globally for agricultural products and commodities. Investment opportunities would tend to be opened and invitations made on a yearly basis for subscription to schemes, which would mature depending on the type of crop. In the case of the forestry sector, contracts would typically foresee a 25 to 30 year duration before the crop would mature sufficiently to enable harvesting. Other crops were more likely to involve short term maturity periods. Two factors in particular are said to have led to the collapses seen in the sector: general lessening of confidence in the aftermath of the global financial crisis and a withdrawal of tax concessions in 2007 that had enabled investments to be offset against tax.\(^{51}\)

Other allegations emerged as a result of class actions filed by the investors against the companies involved and their directors. These included accusations that the prospectuses failed to disclose all the associated risks to investors and that the companies had overstated the value of assets within the schemes, in particular the land and the post-harvesting returns, while understating the liabilities, in particular the cost of future maintenance work on the plantations. Many of these investors had also borrowed moneys from lenders who had specifically set up schemes to finance these investments and, facing claims for the repayment of their borrowings, brought claims of breach of duty of care and unconscionable conduct against those lenders.\(^{52}\)

While the class actions against a number of the companies and lenders have experienced varying fates before the courts, concomitantly, the failure of a large number of businesses in a short time frame prompted a Corporations and Markets Advisory Committee (CAMAC) report into managed investment schemes in July 2012, which recommended, *inter alia*, new governance mechanisms for such schemes and for financially stressed schemes to be assisted towards voluntary administration by new facilitative provisions, while a special liquidation procedure be instituted for insolvent schemes.\(^{53}\)

\(^{50}\) Ibid., section 568F(4).

\(^{51}\) See B. Butler, “Forestry Group faces Class Action” (Sydney Morning Herald, 24 December 2011).

\(^{52}\) Idem.

\(^{53}\) CAMAC Report on Managed Investment Schemes (July 2012), at paragraph 1.6.3.
In the context of the Willmott group insolvency, voluntary administrators had been appointed over companies belonging to the group in October 2010. Concurrently, receivers were also appointed by the group’s lenders. When on discovering the companies in the group were insolvent, including Willmott (Forests) Limited, which was the scheme manager of a number of the schemes, the administrators were then appointed as liquidators in March 2011. In May 2011, the liquidators applied to the Federal Court for directions to include comfort for the position they had reached on their justification for the disclaimer of leases so as to be able to sell the land unburdened by the leases and thus maximise returns for the creditors. They were held so justified on condition they sought consent of the court before making the disclaimers and amending the concomitant scheme documentation to permit disclaimers to take place. They then proceeded to draft contracts for the sale of the land comprised within the various schemes subject to court consent being obtained, these contracts being executed in December 2011. Shortly thereafter, an application was made to the Supreme Court of Victoria for consent, which application was heard before Justice Davies in late January 2012. A preliminary question fell to be determined during the hearing, which was prompted by the intervention of lawyers on behalf of the Willmott Growers Group Inc, an action group representing the investors in the scheme. They had queried whether the purpose of section 568, as Parliament had enacted it, was to enable the disclaimer of leases by the liquidator that had the effect of extinguishing the property rights of the investors, many of whom considered themselves to be tenants under leases, albeit unregistered, language advocating this status having appeared or been suggested, they argued, in the scheme documentation. This depended, of course, on whether the investment contracts had in fact created leases with a proprietary effect, though it seemed both parties were prepared to admit that the agreements conveyed that effect in some, if not all cases.

**Willmott at First Instance: The Traditional View Prevails**

Before the court, counsel for the action group put the proposition, strongly resisted by the liquidators, to the effect that the type of leases contemplated by the law were those that were “property of the company”, as foreshadowed in the opening paragraph of section 568. This necessarily meant that the company could only disclaim leases which were its own property, meaning that where leases had been granted by the company as landlords to investors as tenants, the company had parted with its property and retained only a reversionary interest in the land, the only “property” it could then disclaim. Naturally, support for this position by the court would mean that the sale of the land could not take place in its then present form, since the disclaimer would not expunge the leases off the land. The only solution in such an instance would be for the company to find a buyer for the land as burdened or to disclaim its reversionary interest, in which case the land would escheat to the Crown and it would be then the State’s problem as to what to do with the underlying interests, given that arguably (on one view), as a species of

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54 The facts here are derived from the summaries at the various stages of the Willmott case.

55 Judgment was given on 9 February 2012 and reported as: *Re Willmott Forests Limited* [2012] VSC 29.
merger, escheat would preserve the tenants’ interests as depending on the freehold now vested in the Crown. Alternatively, the tenants could challenge the disclaimer and ask to be “accelerated” in their interests to become freeholders of the property.

In the end, the court went with what was afterwards described as the “traditional position” to the effect that the disclaimer by the landlord of its contractual obligations did not of itself bring the proprietary effect of that contract to an end. For the court, where a tenant disclaimed, whether a tenant did so as lessee or contracting party made no difference, as the act of disclaimer terminated all the tenant’s “rights, interests, liabilities and property”. On the disclaimer happening, the landlord recovered the property as if the tenant had surrendered the lease. If a landlord effected a disclaimer of the lease, this could not operate so as to determine the leasehold interest, which was the tenant’s property, but only the landlord’s “rights, interests, liabilities and property”, however far those extended. This also brought into play a subsidiary issue in the case, which was where on the contract/property continuum leases lay. For the court, a lease was both an inter partes contract and the grant by the landlord of an estate in the land to the tenant with the tenant the owner of that estate. A disclaimer by the landlord could never have the effect of unilaterally extinguishing what amounted to someone else’s property rights. Support was found for this proposition in Re Bastable and Dekala. The contrary assertion in Re Jandowae, where the disclaimer by the landlord’s liquidator was held to have terminated the “correlative” rights of the tenant was distinguished on the basis that the judge in that case “did not illuminate” whether this also meant the property rights of the tenants.

Unsurprisingly, there are proponents and opponents of the judge’s decision. Professor Brown gives more weight to the Re Jandowae decision and is of the view that the contract and lease stand and fall together, while arguing that the Re Bastable and Dekala cases are merely support for the fact that the liquidator, as a trustee, will always take subject to any equities. Some support for the “rolled-up” position can be found in the fact that originally the lease conferred no estate in land, but merely rights enforceable only against the lessee by way of damages. Through a combination of statutory and common law developments, the lease came to be treated as an interest in land protected against the entire world. The lease is then something of a

56 Submission to the CAMAC Enquiry by Counsel for the Growers Group (June 2011), at paragraph 37(b), citing NAB v NSW (2009) 260 ALR 115 as authority. Professor David Brown disagrees with this, stating that the disclaimer of the reversionary interest would simply cause the underlying interests to merge with it: “Disclaimer of Land: seeing the Wood through the Trees” (2012 April) Insolvency Law Bulletin 162, at 164.
57 See A. Robertson, “Can’t see the Forest for the Lease” (28 May 2013) Lavan Legal Publications.
59 Ibid., at paragraph 11.
60 Ibid., at paragraph 9.
64 Brown, op. cit., at 163.
hybrid, involving both the conveyance of an estate in land and a set of contractual rights and obligation that continue to bind the parties throughout the relationship. Difficulties arise when it comes to deciding whether the parties’ relationship should be subject to normal contractual principles or should instead be governed by property principles. In fact, a trend in the past few decades in both Australia and the United Kingdom has been a move away from emphasising the proprietary nature of leases and treating them like other contracts, particularly those in the commercial sector. The courts have on occasion seen no reason why similar fact situations should be treated differently in standard contract (non-lease) and lease situations. Furthermore, they have also held that contractual principles can be extended to lease situations, including implied warranties (of habitability, fitness for use), frustration, mitigation of loss and repudiatory (anticipatory) breach.

Nevertheless, this view is not necessarily universal, as some courts have suggested that the view that landlord and tenant relationship is firmly based in contract has to sit alongside a more conventional analysis of lease arrangement as a conveyance of a proprietary estate. Similarly, the loose language of such agreements is not necessarily determinative. The terms ‘lease’ and ‘tenancy’ refer to contractual aspects of relationship and not necessarily to the consequences (in proprietary terms) of that relationship. However, the problem returns to that simple question of where leases sit as contract and/or as property. Hepburn makes the very valid point that “in some circumstances a right which begins as a contractual right may become a property interest”. The struggle in determining what is contractual, and therefore subject to enforcement in personam, and what is proprietary in nature, upon which in rem rights may be founded, is an old struggle indeed going back to the dawn of English land law and witnessed by the way in which progressively mortgages, leases, restrictive covenants and occupation rights have come up against the contract/property boundary and, in some, but not all, cases been transmuted from purely contractual in nature to becoming “hybrids” with proprietary aspects.

The First Appeal: Contract Wins!

In the Court of Appeal, to where the liquidators naturally took their disquiet at the judgment below, some comfort is given to the idea that the lease, especially the commercial variety of lease, is very much a creature of contract and property, but that its treatment can be “rolled-up” together, as the decision in Tabali clearly showed. As such, the disclamer of the leases brought the

66 Progressive Mailing House Pty Ltd v Tabali Pty Ltd (1985) 157 CLR 17.
68 Bruton v London & Quadrant Housing Trust [1999] 3 WLR 150.
69 See S. Hepburn, Australian Property Law Cases Materials and Analysis (2nd ed) (2012, LexisNexis, Chatswood NSW), at paragraph 1.11.
70 A good discussion of the process is to be found in A. Simpson, A History of the Land Law (1986, Clarendon, Oxford). National Provincial Bank Ltd v Ainsworth [1965] AC 1175 is an example of the House of Lords rejecting Lord Denning’s attempt at creating a “deserted wives’ equity” with proprietary effect.
tenants’ leasehold interests to an end.71 Looking at the context within which the scheme was created and run, the judges were of the view that the “lease”, such as it was, was only part of “a suite of inter-related documents” which regulated the scheme. It was difficult for the judges to regard the investors as having a leasehold interest or estate and their preference would be the view that there was “no demise of the kind that would survive any termination of the very contract that created the tenure”.72 Their view is that to suggest that commercial leases are a demise conferring an interest in land is to ignore the developments adverted to above which suggest a more contractually-based approach to such arrangements.73 In this context also, the disclaimer provisions serve a particular purpose and their use determines the tenancy automatically, thus no acceptance of the repudiation is required as would be required normally.74 The tenants would have the right to claim damages and to prove in the insolvency for the quantum of their loss.

The Second Appeal: Contract Wins Again!

Given the interests and amounts at stake, it was not surprising that one or other side would be unhappy with the appeal judgment. So the matter came to the High Court by special leave to appeal, applied for in September 2012 and granted at a hearing on 10 May 2013. The matter was then argued on 9 August 2013. At the hearing, the essential position of the parties was thus articulated: for the appellants,75 the only property the landlord had was the reversion and if the landlord wished to disclaim this, it needed to bring the reversion under either paragraph (a): “land burdened by covenants” or paragraph (c): “not readily saleable property”. A reversion could not be a contract within the meaning of paragraph (f). As such, to equate the landlord’s interest, even if it went further than a reversion, with the concept of disclaimable contract in the last paragraph was not borne out by the language of the text. Cases such as Tabali which speak of the contractualisation of leases do not assist with this matter, which needs to be resolved by following the canons of statutory interpretation. In any event, leases are more than contracts, but pass property to a tenant. The arrangements under the scheme were equivalent to an executed demise, with all the landlord needing to do being to ensure quiet possession. As such, the tenants had acquired rights which could not be dispossessed by the landlord and which were equivalent to the types of interest seen in Re Bastable, although not registered. The effect of this is to prevent the extinguishing of a lease where the landlord only holds a reversion. Even if this view were incorrect, any disclaimer would only have the effect of determining the landlord’s interest. It could not amount to a repudiation or surrender that affected the tenant’s property. As in Re Bastable and Dekala, if equities could survive, so too would a lease.

72 Ibid., at paragraph 51.
73 Ibid., at paragraph 52.
74 Ibid., at paragraph 47.
75 This section is a summary of the Appellant’s Submissions (filed 14 June 2013) and Reply to the Respondents (filed 19 July 2013).
For the respondent liquidators,\(^{76}\) the disclaimable property included both the reversion, which they accepted would fall under paragraph (a), but also the lease, which is created by contract and would fall therefore within the scope of paragraph (f). Subject to the limitation on court involvement, the inclusion of leases within the category of contracts in that paragraph necessarily means that leases must be regarded, just as contracts, \textit{in toto}. As such, disclaimer terminates both the contractual and proprietary effects of the lease, as the statute effectively contemplates by referring simply to a “lease”. The cases on contractualisation support this, particularly \textit{Tabali}. Where disclaimer occurs and the landlord purports to terminates its “rights, interests, liabilities and property”, of necessity the leasehold interest must fall away, because the tenant is similarly released from its “rights, interests, liabilities and property”. This is particularly true because the lease cannot survive repudiation of the landlord’s liabilities to guarantee the tenant quiet enjoyment and not to derogate from the grant, which are necessary to give efficacy to the leasehold.

The judgment, which came on 4 December 2013, was keenly anticipated.\(^77\) By a 4:1 majority,\(^78\) the appeal was dismissed in language similar to the language of the appeal court below. The High Court interpreted the leases as contracts that fell within section 568(1)(f). This freed the liquidators to sell the reversion unencumbered. As such, the “tenants’ rights to quiet enjoyment and, non-derogation” were terminated and “the tenants are ... left with the right to prove in the winding up as creditors.”\(^79\) Interestingly, in his well-articulated dissent, Justice Keane would have rejected the liquidators’ right to disclaim, ruling firstly that, as the liquidators had not sought the leave of the court pursuant to section 568(1A), the disclaimers were ineffective, and that “if the Liquidators were to disclaim Willmott’s contracts to lease the parcels of land in question with the leave of the court, that disclaimer would free Willmott from further observance of its obligations under the leases, but it would not be effective to deprive the Growers of their right to possession for the balance of the term, to the extent that a court of equity would restrain an attempt to deprive the Growers of their right to possession.”\(^80\) He noted, \textit{inter alia}, that “the scope of the power to disclaim... [is] limited by its focus upon the rights of the insolvent company.”\(^81\) He alone addressed policy considerations; observing that “[s]ince the introduction of the statutory power of disclaimer in 1869, neither judicial exegesis nor academic commentary has attributed to the power of disclaimer the potential to enhance the value of the estate of the company in liquidation, much less to alter the position of those who have dealt with the insolvent by divesting them of rights vested in them.”\(^82\) He also referred to the Harmer Report in support of his conclusion that “as a matter of ordinary language, to speak of ‘disclaiming a lease’ is to speak of disclaiming

\(^{76}\) This section is a summary of the Respondents' Submissions (filed 5 July 2013).

\(^{77}\) Reported as: \textit{Willmott Growers Group Inc v Willmott Forests Limited (Receivers and Managers Appointed) (In Liquidation)} [2013] HCA 51.

\(^{78}\) French CJ, Hayne, Kiefel and Gageler JJ formed the majority, with Keane J in dissent.


\(^{80}\) Ibid., at paragraph 161.

\(^{81}\) Ibid., at paragraph 115.

\(^{82}\) Ibid., at paragraph 125.
a contract which is the property of the lessee."\textsuperscript{83} This would relieve a lessee of an ongoing burden but would leave the landlord free to negotiate with a replacement tenant, including an existing sub-tenant. This approach would provide minimal disruption to commercial arrangements upstream and downstream that the insolvent party had with solvent counterparties.\textsuperscript{84}

**Disclaimers as an Insolvency Issue: Did *Willmott* get it Right?**

Since the judgement appeared, it has been the subject of a certain amount of commentary, chiefly in the professional and "cross-over" publications, where both academics and practitioners write.\textsuperscript{85} It does not appear, however, that the judgement has met with favour. One Australian perspective characterises the judgement as causing "disquiet" because it "ostensibly undermines tenants’ security of tenure." While consonant with the "longstanding purpose of the disclaimer provisions", the extension of the facility in *Willmott* appears to undermine the financing of and taking of security over commercial property.\textsuperscript{86} Citing other professional views, the author notes the usual commercial practice of using disclaimer as a trigger for default with a consequent impact on security enjoyed by the lender, often extinguishing it. Security practices will, as a result of the case, change to require greater consideration of the profile of the borrower and increased due diligence, while further reporting and disclosure obligations may well be imposed. Personal guarantees and options to purchase the property may well be used to supplement the security arrangement, while events of default may well be re-characterised to include breaches of covenants or insolvency happening to the borrower's superior in title. All of these will impose greater "costs, inconvenience and risk." Notwithstanding this, a by-product of the case may well be that liquidators resort more often to the use of such a power to swell the assets available to general creditors. However, and perhaps more importantly, the case leaves unanswered the questions of whether leave is still required for lease disclaimers and what considerations courts will apply in the event of applications being made.\textsuperscript{87} What might occur in scenarios where disclaimers are a realistic possibility is that affected parties may well become pro-active and require liquidators to determine whether to disclaim and may also challenge such disclaimers more readily.\textsuperscript{88}

Commentators in the United Kingdom have been more robust in their criticisms. Cranston and Calland believe that an English court would have decided matters differently.\textsuperscript{89} Anderson states in no uncertain terms that

\textsuperscript{83} Ibid., at paragraph 129.
\textsuperscript{84} This policy is reflected in Ontario in section 39(2), Commercial Tenancies Act 1990.
\textsuperscript{87} Ibid., at 16.
\textsuperscript{88} Ibid., at 17.
\textsuperscript{89} Cranston, op. cit. at 8; Calland, op. cit., at 164.
Willmott is: “from an English law perspective... wrong in principle.” Apart from the differences between the two countries’ legislation, which he argues are material, insolvency law in England would not “regard a leasehold estate as merely a species of contract”, nor would it “permit the adventitious disaggregation of interests for the purposes of disclaimer.” Reasons for this position include the view that disclaimer could not deprive tenants of vested proprietary rights, a situation that might lead to injustice, in the absence of any statutory protection for such tenants.90 A further perspective from practice states categorically that the judgement:

“…impermissibly erodes the concept of security of tenure insofar as it allows a liquidator unilaterally to determine accrued property rights. Effectively leases are then treated as nothing more than contracts. As a matter of commercial analysis, it seems that the property rights in this case were merely incidents of a pure investment scheme, but nevertheless as a matter of law the tenants had acquired property rights which were then stripped away in the insolvency, leaving them with mere money claims.”91

This view is echoed in an Australian journal, where the authors suggest, on a proper reading of the Harmer Report, that the disclaimer provision was never intended to permit the “compulsory forfeiture of proprietary interests.”92 Concerns reflected here are not just about the impact in practice on lending and corollary asset-security arrangements, but raise vital issues about the true nature of the arrangement being entered into. Is it simply about contract or property or both?

The Contract/Property Dichotomy: Willmott’s Part in the Debate

The Willmott debate has brought to the fore the contractualisation debate and the proper place of leases, in particular commercial leases, on the boundaries of contract and property law. A number of issues are raised by this. The dual character of a lease has given rise to conceptual difficulties, as underscored by the divergent judicial approaches adopted in the Willmott litigation thus far. It pays to recall that the judge at first instance in Willmott respected the proprietary interest of the lessee, notwithstanding the operation of the statutory disclaimer. In contrast, the Court of Appeal and the High Court in Willmott endorsed the transmutation of the lease, from its dual character, to one of contractual status. The latter approach, undoubtedly, offers a seductive simplicity in that if the contract goes, the rest goes including the leasehold interest. In such circumstances, the statutory disclaimer facilitates the purpose of a prompt winding up, albeit in a hamfisted way. Some may say such an outcome is perfectly defensible in the context of insolvency. Others may object to the contractualisation of leases in this manner, pointing to the fact that in practice a variety of leases exist and that its use will depend on a multitude of different situations – it can range from the tax driven scheme such as in Willmott, to commercial leases in shopping centres or residential

90 Anderson, op. cit. at 316.
91 XXIV Old Buildings, Insolvency Bulletin (May 2014).
leases. Given that the context and purposes of leases lacks uniformity, it begs the question as to whether a more nuanced approach is required towards the statutory disclaimer of leases. The danger with the High Court’s approach is that it seems to sanction the use of the statutory disclaimer provisions of leases as a blunt tool. It may be questioned whether Parliament intended to interfere with vested rights – the rights accrued to the lessee, such as possession and quiet enjoyment. In this regard, the consequences of Willmott are to render the process by which property interests are given effect more uncertain.

*Willmott* may also be seen as a stage in the debate about the proper boundaries between contract and property. English law, it is said, has always had a *numerus clausus* approach to the recognition of estates and interests. In this “catalogue”, the construction of proprietary relationships can only be done through the use of the “conventional building blocks” the law provides. When one examines the list the Grays provide, however, “mortgages”, “terms of years absolute” (leases) and “restrictive covenants” leap out as being originally contractually founded interests that now have recognised proprietary effect, although this was not always the case. A case may also be made for “easements” and “profits à prendre”, often created through contract, although the law, widely held to derive from the Roman law of servitudes, tends to classify these as real interests once created. The authors do acknowledge, nonetheless, that the categorisation of what constitutes a proprietary entitlement may be “loosen[ing] up”, thus possibly foreseeing the extension other categories of interest. In that light, they also postulate that the frequent bids being made by contractual licences for inclusion within the catalogue “must surely one day succeed”, suggesting that the *numerus* might actually be *apertus*, rather than *clausus*. However, evident within this debate is that the transition appears to be one-way, from contractual to proprietary. None of the interests appear to have retrogressed.

What *Willmott* appears to suggest, however, is that some interests will be downgraded if they are deemed to require primacy to be given to the contractual aspect of the relationship. This is not a novelty, given the contractualisation debate referred to earlier and also the tendency to give effect to contractual arrangements if this reflects the commercial nature of the bargain. However, one cannot help but reflect that, as Hepburn articulates it:

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93 An example given by a number of the attendees at the talk was the retirement village scheme, the question being what might happen to the unit purchasers in the event of the management company’s insolvency.
95 Ibid., at paragraph 1.7.15.
96 Simpson, op. cit. (*in extenso*).
97 Gray and Gray, op. cit., at paragraph 1.7.14.
98 *Malayan Credit Ltd v Jack Chia-MPH Ltd* [1986] AC 549, a case in which business tenants taking a joint tenancy of premises at law were presumed to intend holding as tenants in common in equity, thus reflecting what was viewed as being the typical “commercial” bargain.
“the existence of a contract does not mean that the relationship can never be regarded as proprietary. It is possible for the relationship to confer both contractual and proprietary rights.”

This statement can also be understood insofar as such relationships confer both types of rights, something more than simply a “commercial” characterisation is required to divest the relationship of its proprietary character. In that light, the High Court’s determination is possibly erroneous, but can also be seen as reflecting the “duality” of such arrangements and the desire to give more weight to the contractual aspect of the bargain.

The Law of Unintended Consequences: A Wider Possible Application of Willmott

The tension between liquidators and tenants in the disclaimer context is not just of concern in the managed investment scheme sector, but has application elsewhere in other fields involving contractual relationships dealing with property interests. Business format franchising is a complex, contract-based environment that has gained increasing acceptance since the mid-1990s. In the case of business format franchising, for instance, a franchisor will commonly enter into a head lease of premises and then grant a franchisee the right to establish its business in the premises. The franchisee’s tenure is established by way of a sub-lease or licence. The franchise will be granted in a separate contract, the franchise agreement of potentially long duration. The franchise agreement includes a right for the franchisor to terminate it if the franchisee enters insolvent administration but this right is rarely reciprocal. Executing a franchise agreement triggers the investment by franchisees of considerable sunk sums in fitting out their shop, restaurant or hotel premises. Establishment of their business involves franchisees in many additional contracts (with suppliers, employees, financiers) that are not expressed to be contingent on the franchisor’s continuing solvency. It is not uncommon for franchisors to become insolvent, but for the franchisees’ businesses to be solvent, and viable if freed of the franchise agreement. The franchisor’s liquidator may disclaim the franchise agreement when it is concluded that the franchisor’s business cannot be sold as a going concern, but in a situation analogous to Willmott, the franchisees’ businesses and their investment in physical premises provide them with rights that may be recognised as rights in rem. Once the franchise agreements are disclaimed a burden on the franchisor’s insolvency estate is removed. The remaining burden is the head lease. This may have already been breached by the franchisor failing to pass on to the landlord moneys paid by franchisees for rent and outgoings. Franchisees are not creditors of the franchisor in respect of the upfront part of their investment, the costs sunk in fitting out their premises. If disclaimer of the head lease removes not only the franchisor’s ongoing contractual liability (the burden) but the franchisee’s interest in the premises entirely, leaving the landlord with empty premises instead of a viable tenant, and the franchisee

potentially with its own insolvency, it is hard to see this as a sound or intended outcome of the disclaimer process.

A further unintended consequence is that the insolvent estate is enriched by the liquidator’s ability to disclaim the onerous contract and then to re-sell the interest of the non-breaching party and to apply the proceeds of sale for the benefit of the insolvent party’s creditors. In *Willmott* this meant the liquidator was now free to sell the land formerly encumbered with the management agreements. The purchaser obtained the benefit of the trees which it could mill and sell. In the case of a business format franchise the franchisor’s liquidator can re-sell the franchise opportunity without having to compensate the original franchisee directly. In theory the investors in the forestry scheme, and the disenfranchised franchisees could claim as unsecured creditors but in practice this would yield them a far smaller sum in compensation than the liquidator obtained in the sale of the disclaimed property. An action for unjust enrichment could be pursued by franchisees in this situation. A franchised business is, by its nature, highly geographically dispersed and consequently it is unlikely the franchisees could move quickly enough.

**Conclusions**

In light of the judgment of the High Court, some questions remain. Firstly, is this simply an issue of definition? The Court of Appeal stated that these complex commercial arrangements might not have any proprietary effect at all and could not be regarded properly as estates in land. If they in fact do not, as the High Court also determined, then perhaps the question is conclusively resolved. As contracts, they can simply be disclaimed, leaving the investors to elect to challenge the disclaimer or to prove what losses they may have incurred as unsecured creditors in the insolvency. If, however, they remain estates (as the limited commentary thus far seems united in saying), albeit unregistered, and thus taking effect only in equity, then three questions are raised. The first is: what property is thereby left to the landlord to disclaim? If the landlord has truly parted with the leasehold estate and it is the tenant’s property, does this mean the only thing left to the landlord to disclaim is the reversion? On one view (the investors) this is the case, on the other (the liquidators) it is not. The second question would be, even if the reversion were the only such property, could the lease in any event be disclaimed by treating it as a contract under paragraph (f)? For the investors, the word lease here could only include a lease that was the company’s property. For the liquidators, the word lease was not qualified in the statute and could mean any lease to which the debtor was a party, akin to what would happen in contract. This brings to the fore a third question: always assuming that the landlord could disclaim a lease, what would be the effect of the disclaimer? For the growers, despite the cases that speak of the contractualisation of

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101 With or without court involvement, depending on whether they are “unprofitable”. In the United Kingdom, unprofitability also needs to be evidenced and requires proof of more than just a bad bargain: *Re SSSL Realisations (2002) Ltd* [2006] EWCA Civ 7, at paragraph 36, adopting the five principles with respect to determining this outlined by Justice Chesterman in *Transmetro Corporation Ltd v. Real Investments Pty Ltd* (1999) 17 ACLC 1,314, at paragraph 21.
leases, simply disclaiming the lease only brought its contractual aspects to an end and did not disturb its proprietary aspects: the grant of the estate that had occurred by means of the same contract. For the liquidators, both stood or fell together. This was necessarily so because of the trend for contractualising leases that is amply supported in the jurisprudence, particularly in relation to arrangements with commercial overtones.

There are a number of difficulties that are not clearly dealt with in the High Court judgement. Firstly, does the contractualisation of leases evident in the case-law necessarily lead to the position that a disclaimer of a contract brings to an end any and all proprietary effects of that contract? In fact, had the leases been registered, the indefeasibility provisions of the property statutes would not permit the transactions to be so casually unwound. Where the leases were not registered, would this merit any different a treatment? If, as the court suggests, the questions are to be answered in the affirmative and the disclaimer has that effect, there is an obvious risk. Such a treatment would expose grantees of leases to the risks of their grantor’s insolvency. Does this affect all types of grantees? In particular, would this mean that residential tenants bore the same risks in the event of their landlord’s insolvency as commercial tenants or investors under managed investment schemes? Second, should the possibility of disclaimer be confined to commercial leases or should it extend to all leases? Whereas many commercial leases are genuinely negotiated, many others are standard form contracts. Franchise agreements, too, are standard form contracts where, as noted earlier, it is rare for a franchisee to be able to successfully negotiate inclusion of an ipso facto clause that permits the franchisee to terminate its franchise agreement on the insolvency of the franchisor.

Third, beyond the case of Argyle Gravel, which concerned a superannuation fund, there is no evidence that aggrieved counterparties in Australia have in fact used the challenge to a disclaimer provision available under section 568E(5) of the Corporations Act 2001 on the basis that the disclaimer “has caused, or would cause… prejudice that is grossly out of proportion to the prejudice that setting aside the disclaimer… would cause to the company’s creditors.” In situations like Willmott, and in business format franchising, the directors and their funding sources are often aware of the financial challenges facing the future insolvent party long before the investors or franchisees become aware that their investment is threatened by insolvency. Is it, then, equitable for those “in the know” to benefit from a greater level of security than investors or franchisees? By backing investment opportunities known to be failing, and by encouraging franchisees and other

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102 The authors are indebted to Alex Welch of Henry Davis York for this observation. In practice, where the landlord is the owner of, for example, a large shopping complex, the landlord tends to discourage tenants from entering registrable leases on the title as it makes it cumbersome for registered proprietors to conduct their business.

103 See above note 39.

104 See, for example, A. Ferguson and R. Williams, “Victims seek olive branch from ANZ over Timbercorp collapse” (Sydney Morning Herald, 8 November 2014). See also J. Buchan, “Franchising: A Honey Pot in Bear Trap” (2014) 34(2) Adelaide Law Review 283, at 312, identifying 3 franchisors knowingly trading while insolvent for up to 18 months before the administrator’s appointment.
investors to borrow money to buy these opportunities, these parties risk prosecution by investors or regulators for mis-selling products and for financial malpractice.

The prospects of a wholesale disruption of the leasehold sector with the introduction of both unintended consequences and these added risks, new and unanticipated for many, might lead to a loss of certainty and predictability in the leasing sector and result in financial institutions reassessing, perhaps unfavourably, the risks of lending. In this case, the most obvious next question is whether, to palliate these problems, a distinction could be made between commercial and non-commercial situations with contracts being “rolled-up” in the former, while tenants in the latter category might benefit from some different treatment, whatever that might be? The difficulty here, of course, is that once a definition is attempted, there will undoubtedly be difficult examples that do not fit neatly in one or other category. In the last analysis, the Willmott case has thrown up the ambiguity of the wording of the statute. Is this not an ideal time, therefore, to amend the text to ensure greater clarity and to make proper regulation, should this be desirable, for certain categories of property?

31 August 2015 (revised 20 April 2016)

105 Another contentious example is the retirement village scheme commonly found in Australia, the question being what might happen to the unit purchasers in the event of the management company’s insolvency.

106 McCoy, op. cit., at 14, refers to the editorial comment in A. Lang et al., Lang’s Commercial Leasing in Australia (2013, CCH, Sydney), at paragraph 85-403, which states: “it falls to the legislature to amend the disclaimer provisions in the Corporations Act 2001… if it wants to restore the traditional meaning of disclaimer.”