

## Ask and You May Receive: Equitable Liens, Administrators and Court Directions

### IN SHORT

**The Background:** The administrators of an Australian auction house and gallery business applied to the Federal Court of Australia for directions to recover in excess of \$1 million in fees and costs incurred with respect to performing a stocktake of the auction house's inventory and returning consigned goods to owners.

**The Issue:** Did an equitable lien exist over the consigned goods in favour of the administrators for their fees and costs and, if so, could the administrators recover those fees and costs?

**The Answer:** An equitable lien did not exist over the consigned goods. The Federal Court of Australia also indicated that the administrators could have applied for directions concerning these matters prior to incurring their fees and costs.

The right of administrators to claim an equitable lien over consigned goods and to seek directions from the court under the *Corporations Act 2001* (Cth) was recently considered by the Full Court of the Federal Court of Australia. The decision serves as a timely reminder to insolvency practitioners about when equitable liens may exist and that it may be better to seek directions from the court prior to embarking on certain significant and costly tasks.

Mossgreen, an auction house and gallery business, held approximately 7,000 lots on consignment for more than 800 consignors as well as abandoned items. Mossgreen had no title or legal interest in this inventory and was a bailee of these items. Much of the inventory had been abandoned and was of little value.

The administrators engaged an external party to assist with an investigation of Mossgreen's inventory management system and then to perform a full stocktake of the auction house's inventory. On completion of the stocktake, the administrators issued a circular notifying consigning owners that the administrators held an equitable lien over their goods and that the goods would be returned to them on payment of a \$353.20 levy per lot. In some instances, the levy exceeded the estimated value of the consigned goods.



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The administrators subsequently applied to the Federal Court for directions to recover their fees and costs, claiming that the stocktake was a necessary consequence of Mossgreen's insufficient inventory management systems and that an equitable lien existed over the consigned goods for the expenses incurred in performing the stocktake.

The Federal Court dismissed the application, finding that the administrators had intermeddled with others' goods in circumstances where they had not been requested to do so. The Federal Court found that the work undertaken by the administrators in performing the stocktake did not relate to property owned by Mossgreen or the administration of its affairs.

The administrators appealed the decision to the Full Court in *White, in the matter of Mossgreen Pty Ltd (Administrators Appointed)* [2018] FCAFC 63. For different reasons, the Full Court dismissed the administrators' application.

#### The Full Court's Holding

The Full Court explained that there is a potential entitlement to an equitable lien with respect to work done by administrators when securing and returning consigned property. However, whether this equitable lien is available will turn on the circumstances of each case, including whether the consigned goods are returned under an efficient process proportional to the nature of the goods.

The Full Court held that an equitable lien did not arise in this case because:

- the unique nature of the consigned goods, and the employees' specialist knowledge, made it possible for the consigned goods to be returned without the need to perform the stocktake;

- even if a stocktake was needed, that need arose from Mossgreen's breach of its obligations (as bailee of the goods) to maintain an adequate inventory system. As such, the costs of such exercise should not be passed onto the consignors ahead of the general creditors; and
- much of the costs that the administrators sought to recover had been incurred for the benefit of the general body of creditors who had an interest in preserving the engagement of employees, exploring the possibility of a deed of company arrangement and performing a stocktake for the purpose of being able to demonstrate the extent of consigned goods that a potential buyer of the business might take on for sale by auction. By contrast, the consignors were not interested in those outcomes.

The Full Court also noted that the administrators had sought directions from the Court only *after* they had incurred the costs claimed with respect to the stocktake. This made it difficult for the court to determine on the evidence whether the administrators had considered all relevant options available to them, including whether conducting the stocktake was the most efficient method of returning the consigned goods, proportionate to the value of those goods. The Full Court indicated that it would have been more appropriate for the administrators to have sought directions prior to the administrators undertaking the stocktake.

## TWO KEY TAKEAWAYS

1. Administrators and liquidators may be entitled to an equitable lien with respect to work done when securing and returning consigned property. However, the existence of an equitable lien will be determined by the particular facts of each case, including whether the cost of returning the goods is proportionate to their value.
2. When there is any doubt about a legal position, insolvency practitioners should consider seeking directions from the court under the *Corporations Act 2001* (Cth) prior to taking action. It may be more difficult to obtain directions after action is taken.

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