

Australia: The Arrium Series (#8) - Secondary debt trading - assignments of debts and rights of recovery in Australia

The Arrium Series

Welcome to issue #8 of our **Arrium Series**, where senior members of the Baker McKenzie team involved in the successful defence of proceedings against the former CFO, former Treasurer and other former employees of the Arrium Group, consider key issues arising in those and related insolvent trading proceedings and from the judgment handed down on 17 August 2021.¹

A summary of the relevant background to the Arrium proceedings, some key terms and the key issues to be considered in this **Arrium Series** can be found in **issue #1**, **issue #2** (which considers solvency in the context of large debts due in the relatively distant future), **issue #3** (which considers when and how duties of care may be owed to lenders), **issue #4** (which considers when company directors and employees may be personally responsible for representations), **issue #5** (which considers the interpretation and application of Material Adverse Change clauses), **issue #6** (which considers issues in reliance and causation) and **issue #7** (which considers novel assessments of loss for negligence, misleading conduct and insolvent trading).

Today's issue - Secondary debt trading - assignments of debts and rights of recovery in Australia

This final issue in our **Arrium Series** considers whether rights to sue third parties (causes of action) are assignable under Australian law where a debt has also been assigned and is particularly relevant to anyone engaged in secondary debt trading.

Assignment issues in Anchorage Proceedings

The Lender Proceedings concerned a series of syndicated and bi-lateral facility agreements. In the Anchorage Proceedings, claims were brought against Arrium officers and employees by two banks which lent money to Arrium borrowers ("**Par Lenders**"), as well as by plaintiffs who had taken assignments of debts at a discount to their face (or par) value, either directly or indirectly² from banks who had lent money to the Arrium borrowers ("**Assignee Plaintiffs**").

Broadly, the Anchorage Plaintiffs' claims alleged misrepresentations. Unlike the Par Lenders, who alleged both negligence and breach of the statutory prohibition against misleading conduct in s 18 of the Australian Consumer Law (ACL), the Assignee Plaintiffs were **limited** in their claims to allegations of negligence (which required them to establish that the employees owed a duty of care to the original lenders from whom the assignments were derived) because it is plain that causes of action for

¹ *Anchorage Capital Master Offshore Ltd v. Sparkes (No 3); Bank of Communications Co Ltd v. Sparkes (No 2)* [2021] NSWSC 1025

² through intermediary assignees



damages for breach of s 18 of the ACL are not assignable because s 236 of the ACL does not contemplate an award of damages in respect of loss not suffered by a party to the proceeding.³

Form of assignment

The Arrium debt assignments were effected using the global standard terms issued by the Loan Management Association for "par and distressed trade transactions insolvent bank loans and claims" ("**LMA Standard Terms**").

The LMA Standard Terms provided both for the assignment of the bank loans and also (so-called) "Ancillary Rights and Claims", which were, in effect, defined as claims the Seller (including any predecessor in title) had against any borrower, guarantor or "any other person" that were based in any way, arose out of or related to the assigned bank loans.

The Assignee Plaintiffs relied on this purported assignment of "Ancillary Rights and Claims" to contend that rights the original assignor lenders allegedly had to sue defendants for negligence had been validly assigned to them at the same time as they took assignment of the debts.

Each of the defendants denied that the assignments of "Ancillary Rights and Claims" were effective to enable the Assignee Plaintiffs to bring claims against them on the grounds that the assignments were void as against an Australian public policy which provided that (so-called) "bare" causes of action are not assignable since they savour of, or were likely to lead to, "maintenance".⁴

Previous interlocutory judgment on assignment issues and application for leave to appeal

The efficacy of the assignments of "Ancillary Rights and Claims" was the subject of an earlier interlocutory judgment in the context of an amendment application brought by the Anchorage Plaintiffs to join Arrium's CFO as a defendant to the proceedings⁵ and in an application for leave to appeal from that judgment⁶, where the test, at that stage, was merely whether it was arguable that the assignments were effective.

In that interlocutory judgment, the Court, in allowing the amendments and joining the CFO to the proceedings, decided that:

- the assignment of claims which are ancillary to a proprietary right or interest which is itself assigned was a recognised exception to the general principle prohibiting the assignment of a bare cause of action; and
- on the state of the current authorities, it was at least arguable that the causes of action on which the Anchorage Plaintiffs sued were "ancillary" to the debts assigned to them because "ancillary" in this context included cases where there was "a legitimate commercial purpose in taking an assignment of the causes of action together with the debt".⁷

The CFO's application for leave to appeal from that interlocutory judgment was refused by the NSW Court of Appeal, including because the public policy underpinnings of the prohibition against the assignment of bare causes of action "could not be regarded as secure, or at least not so secure as to justify summary dismissal", on the basis of existing authority in light of:

³ the Arrium Judgment notes, at [483], that it was "common ground that the assignments were not effective to assign any of the statutory causes of action, since it is accepted that the relevant statutes do not permit an assignee to recover damages for a contravention of those provisions"; see also authority referred to in *Anchorage Capital Master Offshore Pty Ltd v Sparkes* [2019] NSWSC 384 (**Anchorage v. Sparkes**) at [19]

⁴ Arrium Judgment at [483] citing *Glegg v. Bromley* [1912] 3 KB 474 at 489 per Parker J

⁵ see *Anchorage v. Sparkes*

⁶ see *Bakewell v. Anchorage Capital Master Offshore Ltd* (2019) 372 ALR 349; [2019] NSWCA 199 (**Bakewell v. Anchorage**)

⁷ Arrium Judgment at [484]



- the abolition of the tort and offence of maintenance and champerty in recent decades; and
- cases⁸ which "appeared" to have reduced the force of prior public policy restrictions based on maintenance and champerty.⁹

The result was that the issue of whether the assignments were effective (as opposed to whether it was merely at least arguable) was contested at the trial of the Anchorage Proceedings and subsequently considered in the Arrium Judgment.

Court findings

Having already concluded that the Assignee Plaintiffs' claims were unsuccessful for a number of other reasons which we have considered in prior issues of this **Arrium Series** (see above), it was ultimately not necessary for the Court to determine the assignment issue in the Arrium Judgment.

Moreover, the Court commented on the difficulties in determining the validity of the assignments without having determined that the Assignee Plaintiffs had a valid cause of action against the defendants, noting that "it seems better that the question of the validity of the assignments be dealt with on the basis of actual findings concerning the causes of action that exist rather than on the basis of one or more of a number of hypotheses" and that it "is arguable, for example, that there is a difference between causes of action which depend on accessorial liability for breaches of obligation arising from the facility agreements and direct claims in negligence against the defendants themselves."¹⁰

However, the Court said that had it been necessary it "would have concluded that the assignments of the causes of action based on representations made in, or by reason of, the Draw down Notices were valid".¹¹

In reaching that conclusion, the Court considered what it regarded as the **legal principles** before and after the seminal decision of the House of Lords in *Trendtex Trading Corporation v. Credit Suisse* [1982] AC 679 (**Trendtex**) and the High Court of Australia's subsequent decision in *Equuscorp Pty Ltd v. Haxton* (2012) 246 CLR 498; [2012] HCA 7 (**Equuscorp**) as follows:

	Comments in Arrium Judgment on relevant principles at particular points in time ¹²
Prior to Trendtex	Two exceptions to general principle that "bare" causes of action not assignable, being where: <ol style="list-style-type: none"> 1. the cause of action is "ancillary" to an assigned property right or interest; or 2. an assignee has a "genuine commercial interest in taking the assignment". Not necessarily a clear dividing line between those two exceptions.
In and following Trendtex	In <i>Trendtex</i> , the House of Lords held, in what was generally seen at the time to be an extension of the existing law, that the second exception (genuine commercial interest in taking the assignment) was wide enough to cover a case where the assignee had a financial interest in the outcome of the assigned claim because its ability to recover a debt owed to it by the assignor depended on the success of that claim.
In and following Equuscorp	<ul style="list-style-type: none"> • <i>Trendtex</i> was accepted as correct by the High Court in <i>Equuscorp</i>. • Also in <i>Equuscorp</i>, the High Court determined that a restitutionary claim had been validly assigned in conjunction with the assignment of a contractual debt, with French CJ, Crennan and Kiefel JJ explaining their decision in these terms, at [53]: A restitutionary claim for money had and received under an unenforceable loan agreement is inescapably linked to the performance of that agreement. If assigned along with

⁸ including *Campbells Cash & Carry Pty Ltd v. Fostif Pty Limited* (2006) 229 CLR 386; [2006] HCA 41 where the High Court held litigation funding was not contrary to public policy

⁹ see *Bakewell v. Anchorage* at [50] (per Bell P, with whom Macfarlan and White JJA agreed) referencing what the plurality in *Equuscorp Pty Ltd v. Haxton* (2012) 246 CLR 498; [2012] HCA 7] described at [50] as "[t]he attenuated role of maintenance and champerty" and decisions such as *Campbells Cash & Carry Pty Ltd v. Fostif Pty Limited*

¹⁰ Arrium Judgment at [486]

¹¹ Arrium Judgment at [486]

¹² from the Arrium Judgment at [487] - [488]



	Comments in Arrium Judgment on relevant principles at particular points in time ¹²
	<p>contractual rights, albeit their existence is contestable, it is not assigned as a bare cause of action.</p> <p>Neither policy nor logic stands against its assignability in such a case. The assignment of the purported contractual rights for value indicates a legitimate commercial interest on the part of the assignee in acquiring the restitutionary rights should the contract be found to be unenforceable.</p> <ul style="list-style-type: none"> • Their Honours in <i>Equuscorp</i> are to there be understood assaying that "a proprietary right and other rights assigned with it will be sufficiently connected to support the assignment of the latter if it can be said that the assignee has a genuine commercial interest in taking an assignment of the latter with the former." • <i>Equuscorp</i> also recognises that there has been a "change in public policy away from the view that 'trafficking' in litigation was a social evil towards a recognition that the assignment of legal rights performs a useful social function in ensuring that losses are properly borne by those legally responsible for them."

In applying those principles following *Equuscorp*, the Court in the Arrium Judgment held that:¹³

- it "seems clear" that the claim of negligence against the Arrium Entities, which, if they existed, underpinned the accessorial liability claims made by the Assignee Plaintiffs against the CFO and Treasurer, were assignable with the assigned debts "since they would have been available as an alternative to a claim based on the facility agreements themselves";
- it then seemed like a "small step" from that conclusion regarding the assignability of claims in negligence against the Arrium Entities, to conclude that the Assignee Plaintiffs also had a "legitimate commercial interest" in the assignment of:
 - accessorial liability claims in relation to breaches of the facility agreements and the representations made in the Draw down Notices by the Arrium Entities, given "the intimate connection between those claims and the claims against the Arrium Entities" and that "those claims were a way in which the Assignee Plaintiffs could protect their position in the event that they could not recover directly against the Arrium Entities"; and
 - direct claims against the defendants in the Anchorage Proceedings "arising out of the same facts for the same reasons"; and
- if the defendants were liable to the Par Lenders as a result of their conduct in connection with the facility agreements, "there appears to be no policy reason why they should not also be liable" to the Assignee Plaintiffs.

In considering evidence of analysis undertaken by at least some of the Assignee Plaintiffs which indicated that, in assessing the price they were willing to pay for the assigned debts, they "placed value on recovery under the defendants' Directors and Officers Liability insurance", which was relied upon by defendants in support of their contention that the assignments were contrary to the public policy against trafficking in litigation, the Court held that:¹⁴

- the Assignee Plaintiffs "acquired debts with a certain face value at a discounted price reflecting the costs and uncertainties associated with the recovery of those debts" and that "if the price they paid for the debts was less than the amount they ultimately recovered, they would make a profit"; but
- this did not, however, establish that they acquired a bare right to sue with the intention of making a profit where:
 - they acquired debts of a certain value;
 - the right to sue was "ancillary to the acquisition of those debts and was one of the means by which the Assignees could seek to recover the face value of the debts that they acquired";
 - there was "no possibility of recovering more"; and

¹³ Arrium Judgment at [489]

¹⁴ Arrium Judgment at [490]



- "[a]ccepting that the trafficking in bare causes of action with a view to profit is still against public policy", the acquisition of the causes of action arising from the Draw down Notices did not fall into that category, although it may be that other causes of action relied on by the Anchorage Plaintiffs did.

Five key takeaways

In summation, the five key takeaways from the Arrium Judgment and cited cases on the issue of assignments of claims against third parties are as follows:

1. Assignment of Australian statutory causes of action for misleading or deceptive conduct are **ineffective** because the relevant statutes do **not** permit an assignee to recover damages for a contravention of those provisions.¹⁵
2. Despite doubts expressed by the New South Wales Court of Appeal¹⁶, trafficking in bare causes of action with a view to profit remains **against Australian public policy** albeit with an increasing number of well-recognised **exceptions**, which include:
 - a. assignments of causes of action by liquidators and other insolvency administrators exercising statutory rights to realise property; and
 - b. litigation funding, at least where the litigation funder does not "overstep the line" in exercising inappropriate control over how any proceedings are to be conducted.
3. While it also likely remains the position that the assignment of a bare cause of action remains prohibited (but see 5. below), that is also subject to important exceptions where:
 - a. a cause of action is **ancillary** to an assigned property right or interest; or
 - b. an assignee has a **genuine commercial interest** in taking the assignment.
4. The Court, in the Anchorage Proceedings, held that the Assignee Plaintiffs acquired a sufficient genuine commercial interest in the claims brought against the third party defendants personally:
 - a. even though those claims were acquired **contemporaneously** with the assignments of debts as part of the same transaction; and
 - b. despite prior cases requiring that assignees have a **pre-existing** genuine commercial interest which did not arise from the same voluntary transaction which effected the assignment, a requirement which has been criticised as being both inconsistent with the approach taken to litigation funding and based on "misguided assumptions" as to Australian public policy.¹⁷
5. The Australian public policy position underpinning a continuing prohibition on assignments of bare causes of action is less "secure" on the present state of the authorities than it was in the past¹⁸, including because the High Court recognised, in

¹⁵ see cases discussed at *Anchorage v. Sparkes* at [19], including *Aquatic Air Ltd v. Siewert* [2015] NSWSC 928 at [87] – [88] per Brereton J citing *Boston Commercial Services Pty Ltd v. GE Capital Finance Australasia Pty Ltd* [2006] FCA 1352; (2006) 236 ALR 720, [51]-[52]; *Tosich v. Tasman Investment Management Ltd* [2008] FCA 377; (2008) 250 ALR 274, [37]; *Mijac Investments Pty Ltd v. Graham* (No 2) [2009] FCA 773; (2009) 72 ACSR 684, [31]; *Re Cant (in his capacity as liquidator of Novaline Pty Ltd (ACN 006 622 933) (in liq))* [2011] FCA 898; (2011) 282 ALR 49; (2011) 85 ACSR 31, [19]; *Colorado Products Pty Ltd (in prov liq)* [2014] NSWSC 789; (2014) 101 ACSR 233, [392]-[396]

¹⁶ see the New South Wales Court of Appeal in *Fostif Pty Ltd v. Campbells Cash & Carry Pty Ltd* (2005) 63 NSWLR 203 at 232 per Mason P (Sheller and Hodgson JJA concurring)

¹⁷ see "Assignments of Bare Rights to Litigate" Assessing the Modern Doctrinal Position" by Andrew Cheng 5 June 2014 <https://ses.library.usyd.edu.au/bitstream/handle/2123/12157/Honours%20thesis%20-%20Andrew%20Cheng.pdf?sequence=1&isAllowed=y>

¹⁸ see *Bakewell v. Anchorage* at [50] (per Bell P, with whom Macfarlan and White JJA agreed) referencing what the plurality in *Equuscorp Pty Ltd v. Haxton* (2012) 246 CLR 498; [2012] HCA 7 said at [50]



Equuscorp, "that there has been a change in public policy away from the view that 'trafficking' in litigation was a social evil towards a recognition that the assignment of legal rights performs a useful social function in ensuring that losses are properly borne by those legally responsible for them".¹⁹

¹⁹ Arrium Judgment at [488]



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