

KORDA & ORS v AUSTRALIAN EXECUTOR TRUSTEES (SA) LIMITED
(M82/2014)

Court appealed from: Court of Appeal, Supreme Court of Victoria
[2014] VSCA 65

Date of judgment: 10 April 2014

Date special leave granted: 15 August 2014

On 25 September 2012, the 1st and 2nd appellants were appointed as receivers and managers of the 5th appellant Gunns Limited ('Gunns') and its subsidiaries, including the 3rd and 4th appellants, SEAS Sapfor Forests Proprietary Limited ('the Forest Company') and SEAS Sapfor Harvesting Proprietary Limited ('the Milling Company').

The Forest Company promoted timber plantation schemes to investors ('the covenantholders') under which the covenantholders purchased a covenant that gave them certain rights and interests. The Milling Company was engaged to provide felling and milling services and also to market and sell the timber derived from the plantations. Any proceeds received by the Milling Company from the sale of timber or sale of plantation lands (subject to deductions for the Milling Company's costs and expenses and its commission) was to be paid to the Forest Company. After making its own deductions for further costs and expenses, the Forest Company was required to pay the net proceeds to Australian Executor Trustees (SA) Ltd (the respondent) for the benefit of covenantholders.

The respondent is and has at all times been a trustee for the covenantholders under the terms of a trust deed entered into by it and the Forest Company on 6 March 1964. In about 2008, the Forest Company and the Milling Company were taken over by Gunns Limited. After the takeover, each company encumbered its assets, by way of a fixed and floating charge, to lenders to the Gunns Group.

There is no dispute that when the proceeds from the harvesting of the timber or the sale of plantation lands was handed to the respondent under the terms of the trust deed, those moneys were then held on trust for the covenantholders. The parties disagreed, however, as to whether or not the proceeds from the sale of timber that were in the hands of either the Milling Company or the Forest Company before they were handed to the respondent under the terms of the trust deed were also held on trust for the covenantholders. The receivers and managers contended that before the proceeds were passed over to the respondent the covenantholders had no proprietary interest in the proceeds of the sale of timber, which were subject to the fixed and floating charge.

The trial judge (Sifris J) found that the covenantholders did hold a beneficial interest in the balance of the proceeds from the harvest of the plantations and the sale of plantation land before the proceeds were handed to the respondent.

The Court of Appeal (Maxwell P and Osborn JA, Robson AJA dissenting) dismissed the appeal of the receivers and managers. The majority considered it was a matter of commercial necessity that the investments made by covenantholders not be at risk by reason of extraneous activities of the operating companies. Had there been any suggestion that such a risk existed, prospective investors would have been much less likely to invest. The only risks to which the parties intended that the investors be exposed were risks intrinsic to the enterprise being funded by their investment moneys, that is, the enterprise of acquiring, preparing and planting land, tending and maintaining the timber, and finally felling, milling and selling it. Investors

knew that the investment returns would depend on the commercial success of the forestry operations. They also knew that, in the event of such commercial success, the benefits would be held for them on trust. No investor would have imagined, and the prospectus certainly did not suggest, that the investment returns could be put at risk by reason of any activity of the operating companies outside the scope of the timber production enterprise. The whole tenor of the documentation was to precisely the opposite effect.

Robson AJA (dissenting) noted the absence of any reference to the timber sale proceeds being held in trust before they were paid to the trustee, in circumstances where the parties expressly established a trust in the clearest terms once the timber sale proceeds were paid to the trustee. His Honour thought this was an extraordinary omission on the part of the lawyers who drew the detailed and lengthy scheme documents; if it was intended that the covenantholders were to be protected at all stages by the land, trees, harvested trees and proceeds being held on trust, it would have been so stated. The omission to do so was a strong indicator of the intended nature and structure of the scheme. His Honour concluded that the matters which suggested that the presumed intention of the parties was not to establish a trust outweighed those that suggested to the contrary.

The grounds of appeal include:

- The Court of Appeal erred in finding (by majority) that the timber sale proceeds and land sale proceeds were held by the Forest Company and/or Milling Company on trust for the relevant covenantholders.
- The Court of Appeal ought to have held that commercial necessity did not require that the covenantholders' interests be protected by a trust structure over the timber sale proceeds or land sale proceeds.

The respondent has filed a Notice of Contention on the following ground:

- The conduct and statement referred to in paragraphs 89 to 91 of *Australian Executor Trustees (SA) Ltd v Korda* [2013] VSC 7 and paragraphs 67 and 68 of *Korda v Australian Executor Trustees (SA) Ltd* [2014] VSCA 65 – and particularly the references therein to past practice – ought to have been taken into account, as evidence of acts by the appellant companies subsequent to the creation of the trust which support the existence and scope of the trust as alleged by the respondent.