



Regal Castings: Definitive determination on voidable dispositions defrauding creditors



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In these recessionary times, with insolvency an increasingly common state of affairs, the actions of debtors which defeat the rights of creditors are carefully scrutinised. The decision of the Supreme Court in *Regal Castings Ltd v Lightbody & Ors* [2008] NZSC 87 definitively clarified what is required to trigger section 60 of the *Property Law Act 1952* (Act) in terms of an intention to defraud creditors on the part of the debtor. The Court voided the transaction and allowed creditors access to the assets.

The case is not just significant for creditors. It is a warning to debtors and their advisers. As one commentator notes, "[The] *Regal Castings* case represents a significant danger for clients seeking to avoid creditors through estate planning arrangements, and certainly also some measure of danger for their advisers." ("Is the Trust fortress strong enough?" *New Zealand Law Society (NZLS) June 2009 Trusts Conference*.)

The facts

Mr Lightbody owed Regal Castings for the debts of his company, Capro Three Ltd. There was significant debt owing, for which Mr Lightbody had liability by way of a personal guarantee to the company. While this debt was outstanding, Mr Lightbody and his wife transferred the family home into a trust. The home was the only asset of value. In four years, that debt was completely forgiven. One year later, Capro went into liquidation, with \$165,000 owing to Regal Castings.

A key issue was whether Mr Lightbody's transfer of his joint interest in the family home was an alienation with intent to defraud his creditors, and therefore voidable. The relevant provision of the Act is section 60. It provides:

60 Alienation with the intent to defraud creditors

- (1) Save as provided by this section, every alienation of property with the intent to defraud creditors shall be voidable at the instance of the person thereby prejudiced.
- (2) This section does not affect the law of bankruptcy for the time being in force.
- (3) This section does not extend to any estate or interest in property alienated to a purchaser in good faith not having, at the time of the alienation, notice of the intention to defraud creditors.

Although this section is now overtaken by section 348 of the *Property Law Act 2007*, the transitional provisions require that the old section 60 will apply to transactions prior to the new Act coming into force; so the old section 60 is likely to be active for a considerable time.

The High Court and Court of Appeal both found that Mr Lightbody did not have the requisite intention. The Supreme Court found otherwise.

Intention to defraud creditors

At the recent 2009 NZLS CLE Family Law Conference, it was noted that the Supreme Court found that intention to defraud does not depend on the inevitability of loss. "Nor is it necessary to show that the purpose or motive of the transfer was to defeat creditors. Intent involves the notion of detrimentally affecting or risking the property of others. While Mr Lightbody's purpose or motive in making the disposition was not to defeat his creditor, he nonetheless had the requisite intent, as the circumstances at the time of the disposition were such that he must have known that by disposing of his only asset of value into trust he was exposing his creditors to a significantly enhanced risk of not recovering [what was owed to them]." (Kelly and Peart, 193, NZLS CLE Family Law Conference, 17-18 September 2009).

On the facts, the relevant circumstances enabling the Court to infer an intention to defeat the creditors were:

1. The fact that the personal guarantee was a significant debt, which Mr Lightbody could not repay at the time the home was transferred into the trust.
2. In setting up the trust, Mr Lightbody's explanation for the disposition was poor. He argued it was for his children, to protect them. But from what? He had been advised by his solicitor that one of the benefits of a trust was protection from creditors.



3. Mr Lightbody had a clear intention to hinder, delay, or defeat Regal Castings' recourse to his interest in the house (should it prove necessary for Regal Castings to have that recourse) as:
 - a. Exchanging his interest in the family home for an unsecured debt not repayable for seven years and simultaneously gifting away \$27,000 of the debt was "a disposition under value" (at [60]).
 - b. Secrecy was adopted by Mr Lightbody with Regal Castings, when his company was dependent on Regal Castings' ongoing support. Secrecy is noted as a "well recognised badge of fraudulent intent" (at [61]).
 - c. Mr Lightbody remained in possession of the family home, and was also the discretionary beneficiary of the trust in respect of both capital and income, "another badge of fraudulent intent" (at [61]).

Persuasive precedent

Some commentators believe the dicta of *Regal Castings* is likely to be applicable elsewhere, where a similar intention is required. In particular, they cite section 47(1) of the *Property (Relationships) Act 1976* as "an obvious example, as its wording is very similar, and ... its purpose is to protect creditors from disposition by or agreements between spouses or partners that are intended to defeat creditors' rights" (Grant and Peart, "The Case for the Spouse or Partner", NZLS June 2009 Trusts Conference).

When advising Family Law clients, keep in mind that *Felton v Johnson* (2006) 25 FRNZ 403, the definitive case on section 47, did not find sufficient motive to intentionally defeat the interests of creditors under section 47(1). It may be that *Regal Castings* offers greater scope for judges dealing with section 47(1), or at least provides an alternative route for creditors where the motive to defeat is "harder to find" under section 60 of the Act.

Regal Castings is a lesson for all advisers to carefully query clients with respect to debts and personal guarantees when advising on estate planning and drafting section 21 agreements or other property sharing agreements outside of separation.