IN THE SUPREME COURT OF VICTORIA
AT MELBOURNE
COMMERCIAL COURT
CORPORATIONS LIST

Not Restricted

S CI 2015 1014

SCROHN PTY LTD (ACN 119 777 507) Plaintiff

v

NEWEARTH CONSTRUCTIONS PTY LTD (ACN 005 358 190) Defendant

JUDGE:	Daly AsJ
WHERE HELD:	Melbourne
DATE OF HEARING:	25 May 2015
DATE OF JUDGMENT:	12 June 2015
CASE MAY BE CITED AS:	Scrohn Pty Ltd v Newearth Constructions Pty Ltd
MEDIUM NEUTRAL CITATION:	[2015] VSC 254

CORPORATIONS ACT 2001 – Application to set aside statutory demand under section 459G – Whether genuine offsetting claim under section 459H – Statutory demand based upon judgment obtained pursuant to the *Building and Construction Industry Security of Payments Act 2002* (Vic) – Whether judgment debtor is entitled to raise a cross-claim under the same construction contract to which the judgment debt relates – *Diploma Constructions (WA) Pty Ltd v KPA Architects Pty Ltd* [2014] WASCA 91 considered.

APPEARANCES:	Counsel	Solicitors
For the Plaintiff	Mr J McKay	Beck Legal
For the Defendant	Mr R Andrew	Donaldson Whiting & Grindal

HER HONOUR:

1 The applicant, Scrohn Pty Ltd ('Scrohn') is the developer of a commercial property in Kyneton. In April 2012, Scrohn engaged the respondent, Newearth Constructions Pty Ltd ('Newearth') to carry out construction works at the property in accordance with a contract dated April 2012 ('Contract'). Disputes emerged between the parties regarding various matters. On 24 October 2014, Newearth obtained a judgment in its favour from the County Court of $110,000 plus interest ('Judgment'), being the amount due as the balance of a progress claim pursuant to s 17(2)(a)(i) of the *Building and Construction Industry Security of Payment Act 2002* (Vic) ('Act'). Judge Anderson found that the progress certificate signed by the superintendent appointed under the Contract was a payment schedule within the meaning of s 17 of the Act. Judge Anderson rejected the submissions of Scrohn that the amounts claimed by Newearth were in respect of variations which were excluded from the operation of s 17 of the Act, and Scrohn's contentions that it was entitled to suspend payments to Newearth by reason of the terms of clause 44 of the Contract.

2 Prior to the date of the Judgment, on 18 September 2014, Scrohn issued separate proceedings in the County Court seeking damages and other relief pursuant to the terms of the Contract in relation to the following claims:

(a) a claim for liquidated damages pursuant to clause 35.6 of the Contract by reason of the delay in achieving practical completion under the Contract; and

(b) a claim for reimbursement of payments made by Scrohn to Newearth in respect of excavation of rock at the property, the costs of which Scrohn asserts ought to be borne by Newearth under the terms of the Contract.

3 It is not apparent from the reasons for judgment of Judge Anderson on 24 October 2014 ('Reasons') whether he was aware of the issue of the County Court proceeding. Scrohn's claims in the County Court proceeding were not raised as defences to Newearth's claims under the Act. However, as is apparent from the terms of a letter from Scrohn to Newearth dated 17 October 2013, which was provided to the Court

after the hearing on 25 May 2015 ('17 October letter'), that Scrohn deducted the sum of $114,000 from the amount it paid to Newearth pursuant to Newearth's final invoice, relying upon its claim for liquidated damages. However, that contention was not pressed by Scrohn before Judge Anderson as a basis for resisting Newearth's claims under the Act.

4 On 7 January 2015, the County Court issued a warrant at the request of Newearth in order to enforce the Judgment. Further, on 16 February 2015, Newearth issued a statutory demand in relation to the Judgment, with the amount owing said to be $128,758.50. On 6 March 2015, Scrohn issued an application to set aside the statutory demand pursuant to s 459G of the *Corporations Act 2001* (Cth), which is the application currently before this Court. Shortly after the hearing on 25 May 2015, the solicitors for Scrohn informed the solicitors for Newearth and the Court that Scrohn intended to apply to the County Court to set aside the warrant issued on 7 January 2015 on the basis that it is 'defective and/or misconceived'. However, that proposed application is largely irrelevant to the determination of the current application before the Court.

5 Scrohn seeks to set aside the statutory demand on the basis that it has an offsetting claim within the meaning of s 459H of the *Corporations Act*, the quantum of which exceeds the sum claimed by Newearth in the statutory demand. The total quantum of Scrohn's claims in the County Court proceeding is $229,758.49 (plus interest and costs) along with a declaration that Scrohn is not liable to pay the outstanding balance of Newearth's claims for payment with respect to rock excavation costs.

6 An offsetting claim is defined in s 459H of the *Corporations Act* as:

> a genuine claim that a company has against the respondent by way of counterclaim, set-off or cross-demand (even if it does not arise out of the same transaction or circumstances as a debt to which the demand relates).

7 Scrohn relies upon its claims in the County Court proceeding as being an offsetting claim within the meaning of s 459H as a basis of setting aside the statutory demand. Counsel for Scrohn submitted that there could be no dispute that Scrohn's claims in

the County Court proceeding are 'genuine', in the sense that they are not 'spurious, hypothetical, illusory or misconceived'[1] or 'frivolous or vexatious'.[2] Newearth opposes the application to set aside the statutory demand on the basis that, among other things, all of the matters which give rise to Scrohn's claims in the County Court proceeding are matters which arise from the same contract and construction project which gave rise to Newearth's right to obtain the Judgment. Newearth relies upon the decision of the Court of Appeal in Western Australia in *Diploma Construction (WA) Pty Ltd v KPA Architects Pty Ltd*,[3] which considered the interaction between s 459H of the *Corporations Act* and the Western Australian equivalent of the Act, as authority for the proposition that an offsetting claim can only be raised in an application to set aside a statutory demand if the offsetting claim arises from transactions separate from those that give rise to the judgment debt under the Act.[4]

8 Counsel for Newearth in his oral submissions also submitted that the terms of the Contract did not permit Scrohn to rely upon its claims in the County Court proceeding as a means of evading its obligation to make payments due to Newearth under the Contract and the Judgment. Further, given that the reason originally advanced by Scrohn for withholding payment from Newearth in the first place was Scrohn's claim for liquidated damages, this claim was ultimately subsumed by the Judgment, and as such, is not a genuine offsetting claim, but is rather an attempt to impeach the Judgment.

9 Counsel for Scrohn agreed that *Diploma Constructions* is good law, and that Scrohn would not be able to set aside the statutory demand merely on the basis that it disputed its indebtedness under the Judgment. Rather, he submitted that the relevant question for determination is whether Scrohn's claims in the County Court proceeding are offsetting claims arising from separate facts and matters than those which underlie the Judgment. Counsel for Scrohn relied upon the following passage of the judgment of Pullin JA in *Diploma Constructions* (with whom the other judges of

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1 see *Spencer Constructions Pty Ltd v G & M Aldridge Pty Ltd* (1997) 76 FCR 452 at 464.
2 *Edge Technology Pty Ltd v Lite-On Technology Corp* (2000) 156 FLR 181.
3 [2014] WASCA 91.
4 Ibid at [68].

the Court of Appeal of Western Australia agreed):[5]

> There is no doubt that the recipient of a statutory notice may successfully apply to set aside a statutory demand based on an adjudicator's determination or a consequent judgment if it has offsetting claims arising from transactions separate from those that gave rise to a judgment debt based upon an adjudication under the Act: *Demir Pty Ltd v Graf Plumbing Pty Ltd* [2004] NSWSC 533 (at [17]) (per Campbell J).

10 Counsel for Scrohn also relied upon *Demir Pty Ltd v Graf Plumbing Pty Ltd*[6] as authority for the proposition that notwithstanding the 'pay now, argue later' policy which underlies the Act, which has the object of ensuring that builders are not starved of cash pending the determination of their disputes with their principals, no special treatment is afforded to judgment creditors who are builders when they serve statutory demands under the C*orporations Act.* In *Demir Pty Ltd v Graf Pluming Pty Ltd*, as noted by Pullin JA in *Diploma Constructions Pty Ltd*, Campbell J stated as follows:[7]

> (I)t was submitted that, if it were possible to rely upon an offsetting claim to set aside a statutory demand, the object of the BACISOP Act would not be achieved. I do not accept that this is so. There are means of enforcement, short of a winding up action, which are open to a judgment creditor. When a judgment has been obtained pursuant to the BACISOP Act, if the judgment debtor does not pay it voluntarily, then the judgment creditor can use the range of remedies open to a judgment creditor. It is not possible, however, for the terms of a Commonwealth Act, the C*orporations Act 2001* (Cth), to be construed, or limited, by reference to the intention implicit in a State Act. The provisions of Div 3 of Pt 5.4 of the C*orporations Act 2001* (Cth) set out a regime whereby a statutory demand is set aside whenever there is an offsetting claim, as defined.

11 Counsel for Scrohn also relied upon the decision of Vickery J in *Façade Treatment Engineering v Brookfield Multiplex*,[8] in support of its contention that where the policy underlying the Act conflicts with the policy underlying the insolvency provisions of the C*orporations Act,* the latter must prevail by reason of s 109 of the Commonwealth Constitution.

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5 Ibid at [68].
6 [2004] NSWSC 553.
7 Ibid at [20].
8 [2015] VSC 41 at [80].

12 Setting aside for the moment the arguments advanced by Newearth's counsel that the terms of the Contract preclude Scrohn from seeking to evade payment of the judgment debt, I agree with counsel for Scrohn that a key question in this application is the proper construction of the term 'transaction'. That is, does the term 'transaction', as used by Pullin JA in *Diploma Constructions*, refer to the relevant contract or project as a whole, as contended for by Counsel for Newearth, or, as submitted by counsel for Scrohn, should the word 'transaction' be considered to be synonymous with 'facts' and 'matters', so that disputes arising out of a single contract or project may give rise to an offsetting claim, provided that the party seeking to establish the existence of an offsetting claim is not simply seeking to mount a collateral challenge to the judgment debt?

13 I agree with counsel for Scrohn that *Diploma Constructions* is not authority for the proposition advanced on behalf of Newearth: that is, that the term 'transaction' should be construed so broadly as to prevent a party raising an offsetting claim which arises out of different facts and circumstances than those arising out of the judgment debt, but are in connection with the same construction project, or arise under the same contract. This conclusion is based upon the following:

(a) the passages in *Diploma Construction* which refer to with apparent approval proceedings concerning disputes analogous to the current case, and where an offsetting claim has found to have arisen under the same contract or project; and

(b) the terms of s 459H of the *Corporations Act*.

14 In relation to (a) above, I note that Pullin JA referred with approval to examples of cases where a principal had been found to have a genuine offsetting claim, rather than merely a dispute regarding the validity of the debt which was the subject of a judgment or adjudication in favour of a builder. In *Max Cooper v Booth*,[9] the relevant offsetting claim arose under the same contract under which the builder had obtained

[9] (2003) 180 FLR 318.

a judgment for its payment claim. In *Greenaways Australia Pty Ltd v CBC Management Pty Ltd*,[10] a principal was held to have an offsetting claim when it sought to recover alleged overpayments in relation to invoices which were not those which were the subject of the builder's judgment debt, because those invoices had been paid. While these decisions predated *Diploma Constructions*, the issue of whether these claims arose out of the same or separate transactions, despite being claims under the same contracts that the builders obtained judgments in respect of payment claims was not expressly considered by Pullin JA. However, in dealing with the application before the Court, he stated:[11]

> Likewise, in this case, if the appellant's cross-claim for damages for defective work totalling $287,905.40 is a 'genuine' offsetting claim, it should result in the reduction of the amount of the demand. As already mentioned, whether there is evidence sufficient to establish the genuineness of the alleged offsetting claim is an issue which will be considered later when dealing with the respondent's notice of contention.

15 The statements of Pullin JA above are inconsistent with the contention that an offsetting claim giving rise to a right to set aside a statutory demand cannot arise under or in connection with the building contract under which the builder obtained its judgment. The Court of Appeal rejected the principal's assertion of the existence of an offsetting claim on the basis of a lack of evidence, but not on the basis that claims arising under the same building contract could not constitute an offsetting claim.

16 As for sub-paragraph (b) above, while it is not strictly correct to say where there is a conflict between the policy underlying a Commonwealth statute and a policy underlying a State statute, the policy underlying the Commonwealth statute must prevail (rather, where there is an inconsistency between Commonwealth and State legislation, it is the Commonwealth legislation which prevails), it is noteworthy that no special status is afforded to a judgment creditor who is a builder within the insolvency provisions of the *Corporations Act*. In *Deputy Commissioner of Taxation v*

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10 [2004] NSWSC 1186.

11 at [72].

Broadbeach Properties Pty Ltd ('DCT v Broadbeach')[12] (upon which Pullin JA relied to base his conclusion that a principal against whom a judgment had been obtained could not set aside a statutory demand on the grounds that there was a genuine dispute about the existence of the debt), the High Court stated:

> It is true that s 459G provides for curial decisions to set aside statutory demands and that grants of jurisdiction to superior courts … are not to be construed with limitations without sufficient reason to do so.

17 Furthermore, one must also have regard to the purpose for and context in which the provisions of the C*orporations Act* governing the issuing and setting aside of statutory demands operates: strictly speaking, if not practically speaking, the issuing of a statutory demand is not just a debt collection tool, it is a step which may lead to the recipient corporation becoming insolvent. The purpose of s 459G and s 459H of the C*orporations Act* is to enable a corporation which is put on a path to insolvency by a creditor to remove itself from that path in prescribed circumstances, one of which is the existence of a genuine offsetting claim. The effect of the 'pay now, argue later' regime under the Act has the effect of, as confirmed by *Diploma Constructions*, limiting a principal's ability to dispute the validity of the debt upon which a judgment is obtained by a builder utilising the provisions of the Act, but the authorities make it clear that a genuine offsetting claim may still be raised. It simply cannot be a disguised collateral attack on a judgment obtained by the builder in reliance upon the provisions of the Act (or its interstate equivalents).

18 Finally, the language of s 459H itself is illuminating: it refers to an offsetting claim as

> a claim the company has against the respondent by way of counterclaim, set-off or cross demand (<u>even if it does not arise out of the same transaction or circumstances as a debt to which the demand relates</u>). (emphasis added)

19 The phrase which is emphasised above is expansionary in nature, to encompass claims which arise from all dealings between parties, not just dealings concerning a particular contract or exchange. By implication, the existence of such an expansionary clause seems to me to presuppose that counter-claims, set-offs and

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12 (2008) 237 CLR 473, 493.

cross-claims which arise out of the same transaction or circumstances to which the debt relates may be an offsetting claim within the meaning of s 459H of the *Corporations Act*. Having regard to the language of the statute itself, it must be that the reference by Pullin JA to 'transactions separate from those that gave rise to the judgment debt' ought to be confined to the particular transaction or facts and circumstances underlying the judgment debt. If it is not so confined, it may well be 'plainly wrong'.

20 Having found that the authorities do not preclude a genuine offsetting claim arising under the same contract under which a judgment has been obtained under the Act being a basis for setting aside a statutory demand, the question arises as to whether the claims brought by Scrohn in the County Court proceeding are properly characterised as offsetting claims, and are not a disguised collateral attack on the Judgment. In my view, having regard to the pleadings in both the County Court proceeding and the proceeding which gave rise to the Judgment, Scrohn does have genuine offsetting claims, save that its claim for a declaration that it not be required to pay the amount said to be owing to Newearth in respect of rock excavation costs.

21 Newearth relies upon the 17 October letter as a basis for asserting that Scrohn's claims in the County Court proceeding, at least insofar as they include a claim for liquidated damages for delay, amounts to a collateral attack on the Judgment. This argument is not without foundation, given the terms of the 17 October letter and the close coincidence of the quantum of the Judgment and the quantum of Scrohn's liquidated damages claim. However, it is clear from the pleadings in the proceeding giving rise to the Judgment and the terms of the reasons of Judge Anderson that the question of Scrohn's entitlement to liquidated damages was not agitated in that proceeding as a defence to Newearth's claim for payment under the Act. The liquidated damages claim may have been the motivation for Scrohn withholding payments from Newearth, and the legal basis by which Scrohn asserted it was entitled to do so, but it could not be said that it was a claim that somehow merged in the Judgment. Rather, Scrohn defended the claim by Newearth under the Act on the

basis that:

(a) Newearth's payment claim was not a 'payment claim' as defined by s 14(1) of the Act, because it did not identify or describe the construction works for which the payment claim related, and included a claim for payment for variations which did not fall within the class of claimable variations under the Act;

(b) the Progress Certificate certified by the Superintendent appointed under the Contract was served upon Newearth without the knowledge or consent of Scrohn; and

(c) Scrohn was entitled, by reason of clause 1.10 of the general conditions of the Contract, to suspend payment to Newearth under the Contract by reason of Newearth's failure to carry out works in accordance with the approved construction program under the Contract.

22 It appears from the Reasons that the defence in paragraph 21(b) above was not pursued by Scrohn before Judge Anderson. However, the remaining defences were considered and determined (adversely to Scrohn) by Judge Anderson. Scrohn's claim for liquidated damages for delay were not referred to in either the pleadings or the Reasons.

23 Accordingly, it could not be said that by raising this claim as a ground for setting aside the statutory demand, Scrohn is embarking upon a collateral attack upon the Judgment.

24 Scrohn's position is to be contrasted with that of the principal in *Diploma Constructions*, where the principal sought to argue that a claim in a proceeding where it sought declarations that the contractor was 'not entitled' to the amounts payable under two adjudications under the Western Australian equivalent of the Act. Pullin JA held that, in light of the reasoning of the High Court in *DCT v Broadbeach*,[13]

[13] (2005) 237 CLR 473.

the authorities which held that a party could raise a genuine offsetting claim merely by contending that it is not 'in truth, indebted for the amount' were plainly wrong.

25 Similarly, Scrohn's claim to be repaid the amounts paid by it for the rock excavation works do not seek to attack the Judgment. The amounts paid by Scrohn in respect of rock excavation costs were in respect of payment claims 2, 5 and 6, dated 13 September 2012, 29 May 2013, and 16 July 2013. The amounts under payment claims 2 and 5 (being $40,050 and $39,390) were paid in full. Payment claim 6 sought the sum of $39,966, of which $36,318.49 has been paid. The payment claim upon which the Judgment was granted was not in evidence, but is said to have been dated 28 June 2013. Again, subject to the observations below, the claim in respect of rock excavation costs amounts to a genuine offsetting claim.

26 However, the above statement must be qualified: to the extent that Scrohn seeks declarations in the County Court proceeding that it is not obliged to pay amounts in respect of unpaid rock excavation costs, and that those claims are encompassed in the Judgment, it does not, according to the reasoning in *Diploma Constructions*, qualify as an offsetting claim within the meaning of s 459H of the *Corporations Act*, on the basis that a claim for a declaration is not a claim that is quantifiable in money terms.[14] However, applying that reasoning to Scrohn's claims in the County Court proceeding merely limits the quantum of the offsetting claim to the amounts already paid by Scrohn.

27 No issue was taken by counsel for Newearth that Scrohn had not satisfied the evidentiary requirements to establish the existence of genuine offsetting claims, and indeed, I am satisfied that Scrohn in its affidavit material has done so. However, counsel for Newearth, in his oral submissions, submitted that the terms of s 459G and s 459H of the *Corporations Act* do not alter the right of the parties at common law, and the terms of the Contract prevent Scrohn from asserting any claim against Newearth until the amounts payable to Newearth under the Contract are paid. If Scrohn's offsetting claim is barred by the Contract, then it cannot be a genuine

14 At [78]-[79].

offsetting claim within the meaning of s 459H.

28 Counsel for Newearth relied upon the provisions of clauses 42 and 47 of the Contract. Clause 42.1 of the Contract provides as follows:

> Within twenty eight (28) days after receipt by the Superintendent of a claim for payment or in the case of a Final Payment Certificate, within 28 days of the Superintendent issuing the Final Payment Certificate, the Principal shall pay to the contractor or the Contractor should pay to the Principal, as the case may be, an amount not less than the amount shown in the certificate as due to the contractor or to the Principal, as the case may be. Such payment shall not prejudice the right of either party to dispute under clause 47 whether the amount so paid is the amount properly due and payable and on determination (whether under clause 47 or as otherwise agreed) of the amount so properly due and payable, the Principal or Contractor as the case may be, shall be liable to pay the difference between the amount of such certificate and the amount so properly due and payable.

29 Clause 42.10 of the Contract provides that:

> The Principal may deduct from moneys due to the Contractor any money due from the Contractor to the Principal otherwise than under the contract … (emphasis added).

30 Clause 47.1 of the Contract provides that:

> If a dispute between the Contractor and the Principal arises out of or in connection with the Contract, including a dispute concerning a direction given by the Superintendent, then either party shall deliver by hand or send by certified mail to the other party and to the Superintendent a notice of dispute in writing adequately identifying and providing details of the dispute.

31 It was submitted on behalf of Newearth that the payment and dispute resolution provisions of the Contract in effect mirror the 'pay now, argue later' regime under the Act, and any attempt by Scrohn to escape its obligations to pay Newearth, including its application to set aside the statutory demand, is not permitted by the terms of the Contract. In particular, clause 47.1 requires Scrohn to continue to meet its obligations to pay Newearth under the Contract, notwithstanding the existence of a dispute. The payments in respect of Newearth's claims for payment for rock excavation were made without any notice of dispute being issued by or on behalf of Scrohn, and the terms of clause 42.10 do not entitle Scrohn to set-off, as it signalled in the 17 October letter, any amount which represented a sum claimed by it under the

Contract.

32 I do not find this argument attractive. It is significant that the contention that contractual terms governing payment procedures and dispute resolution terms preclude a party from taking steps to set aside a statutory demand is unsupported by authority. In *Novawest Contracting Pty Ltd v Taras Nominees Pty Ltd*,[15] Gillard J considered payment terms and dispute resolution clauses substantially similar to those in the Contract. He found that these terms precluded a principal from seeking to set-off the amount of any cross-claims from a progress payment under the contract. However, he referred with approval to the following statement of Lord Diplock in *Silbert-Ash (Northern) Ltd v Modern Engineering (Bristol) Ltd:*[16]

> So when one is concerned with the building contract one starts with the presumption that each party is to be entitled to all those remedies for its breach as would arise by operation of law, including the remedy of setting up a breach of warranty in diminution or extinction of the price of material supplied or work executed under the contract. To rebut that presumption one must be able to find in the contract clear unequivocal words in which the parties have expressed their agreement that this remedy shall not be available in respect of breaches of that particular contract. (emphasis added)

33 There is no express term in the Contract to the effect that Scrohn has surrendered its rights under s 459G of the *Corporations Act*.

34 Newearth has relied upon its contractual and statutory rights to obtain the Judgment. It is now seeking to enforce the Judgment, once again utilising its statutory rights. In my view, the terms of the Contract cannot preclude Scrohn from exercising its common law and statutory rights: first in making its claims in the County Court proceeding, and secondly, in relying upon those claims to set aside the statutory demand.

35 Accordingly, given that the quantum of Scrohn's claims exceeds the amount claimed in the statutory demand, I will order that the statutory demand dated 16 February 2015 be set aside and hear from counsel on the question of costs.

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15 [1998] VSC 205.

16 (1974) AC 689, 718.