I have an unsecured debt with a bankrupt - will I get any money back?

Date : June 5, 2023

If you are an unsecured creditor in a bankruptcy, you might be one of the last few creditors to be paid. In some cases, there may be no funds left to be distributed to you once the secured creditors are paid. However, there is a way of increasing your chance of getting some of what you are owed back.

Priority of creditors

The priority of creditors depends on whether a creditor is a secured or unsecured creditor. Secured creditors are those who have a security interest (for example, a mortgage or charge) over some or all of the debtor's assets. Unsecured creditors have no security over the debtor's assets. Unsecured creditors normally rank after secured creditors in the event of a bankruptcy.

When a debtor becomes bankrupt, unsecured creditors must cease chasing the bankrupt for payment of its debts, but they may lodge a proof of debt with the trustee in bankruptcy which sets out the particulars of any debts incurred by the debtor. The trustee in bankruptcy will then accept or reject the proof of debt.

A secured creditor may take possession of a secured asset after an act of bankruptcy and sell it to reduce the value of their debt. If there are any proceeds remaining after payment of secured debts, those proceeds may be given to the trustee in bankruptcy for payment of any unsecured debts.

Section 109(10) of the *Bankruptcy Act 1966* (Cth) ("*Bankruptcy Act*")

An unsecured creditor may invoke the Court's discretion under section 109(10) of the *Bankruptcy Act 1966* (Cth) ("***Bankruptcy Act***") to recover debt from the bankrupt in priority of other unsecured creditors.

Section 109(10) of the *Bankruptcy Act* provides that:

Where in any bankruptcy:

(a) property has been recovered, realized or preserved under an indemnity for costs of litigation given by a creditor or creditors; or

(b) expenses in relation to which a creditor has, or creditors have, indemnified a trustee have been recovered;

the Court may, upon the application of the trustee or a creditor, make such orders as it thinks just and equitable with respect to the distribution of that property and the amount of those expenses so recovered with a view to giving the indemnifying creditor or creditors, as the case may be, an advantage over others in consideration of the risk assumed by creditor or creditors.

This section was recently discussed in the case of *Jones v Robson, as Trustee for the estate of Jones* [2023] FCA 497 ("***the Jones v Robson case***").

The Jones v Robson case

1. *Background*

In this case, David Charles Jones ("**the Applicant**") was a judgment creditor in the bankrupt estate of Jeffery William Jones (also known as Jeffrey William Jones) ("**the Bankrupt**"). Mr William Roland Robson has acted as the trustee in bankruptcy of the estate ("**the Trustee**").

During his bankruptcy, the Bankrupt caused a transfer of a property at Templestow, Victoria ("**the Property**") to Mr Wayne Bonnici. The Bankrupt filed a debtor's petition under a spelling of his name which differed from the name recorded as the registered proprietor of the Property. The Applicant asserted that that the Property should have been included as part of the divisible estate of the Bankrupt. Mr Bonnici asserted that the Bankrupt held the Property as trustee for him.

The Applicant funded the Trustee in the proceedings to recover the property for the benefit of the estate. The litigation was settled on terms that Mr Bonnici would pay an amount of $401,500 inclusive of costs. After deducting costs and administration charges, the Trustee estimated that a balance of approximately $216,663.86 would remain for distribution to the unsecured creditors of the bankrupt estate.

The Applicant applied for priority payment pursuant to section 109(10) of the *Bankruptcy Act 1966* (Cth). The Trustee advised the creditors that he was supportive of this application, but did not intend to participate in this proceedings unless requested to do so by the Court or by the creditors. No creditor responded to the Trustee and no creditor sought to be heard on the application.

1. *The decision*

The Court held that the that the Applicant undertook a significant risk in funding the litigation. Had it not been for the persistence of the Applicant, the Trustee would not have considered the Property as a potential asset of

the bankrupt estate and the litigation would not have been funded to pursue recovery of the Property. It was also significant that the litigation was complex. The Court was satisfied that it was just and equitable to confer an advantage upon the Applicant over the other creditors in the bankrupt estate in consideration of the risk that the Applicant assumed. The Court ordered that the balance of the settlement sum be paid to the Applicant in priority to each other creditor of the bankrupt estate.

What does this mean for unsecured creditors?

This case shows that, although the interests of unsecured creditors are prioritised last, unsecured creditors are provided some protection under section 109(10) of the *Bankruptcy Act*. If you have indemnified a trustee in bankruptcy for the costs of litigation to realise a property, and there has been some recovery on those costs, you should consider applying to court to gain priority over other unsecured creditors.