



# CREDITOR'S STATUTORY DEMAND: FRIEND OR FOE?

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MAY 2016

Creditor's statutory demands ("statutory demands") are often used by creditors as a method of debt recovery – issued to force a debtor company into paying the debt or risk being wound up.

The Courts have cautioned against the use of statutory demands for this purpose, noting that when a debtor company is solvent, the right course is to bring an action for debt, so pursuing a winding up is an abuse of the Court process.

Statutory demands serve a public interest because they tend to discourage or prevent insolvent companies from continuing to trade.

Unsurprisingly, the statutory demand provisions of the *Corporations Act 2011* (Cth) ("Act") are some of the most highly litigated provisions of any legislation in Australia, particularly regarding applications to have them set aside (Sections 459G and 459J).

## BACK TO BASICS

While we recommend having a lawyer prepare and issues a statutory demand, we understand that commercial realities sometimes prevent a creditor from engaging a lawyer. To that end, here are some of the basic considerations for preparing and serving a statutory demand.

## FORM

For a statutory demand to be properly made it must:

1. be in writing;
2. be in the prescribed form (Form 509H in Schedule 2 of the Act);
3. be signed by the creditor;
4. if it relates to a single debt, then specify the debt and the amount. If it relates to 2 or more debts, then specify the total amount of the debts. (Either way, the amount must be over \$2,000);
5. require the company to pay the debt within 21 days after the demand is served; and
6. be accompanied by an affidavit verifying the debt, where the debt is not a judgment debt.

A statutory demand should be expressed in clear, correct and unambiguous terms. If not, then the creditor may not be able to rely on it to prove insolvency for the purposes of a winding up application.

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### WHO CAN MAKE THEM?

A creditor can serve a statutory demand in relation to a debt that the company owes to them. The term "debt" has been described as "a liquidated sum of money presently due, owing and payable by one person, called the debtor, to another person called the creditor", including judgment debt.

Relevantly, statutory demands cannot be issued in respect of unliquidated sums, a right to damages for breach of contract and various other categories.

### SERVICE

Once the statutory demand is prepared, it must be served in accordance with the Act. While we normally recommend personal service on the Director, it is possible to serve a statutory demand by leaving it at or posting it to, the registered office of the company.

There are hundreds of cases on invalid service, including one where the demand was set aside because the post code was obscured on the envelope which contained the statutory demand.

Service has also been considered invalid where the relevant documents were simply left in a letterbox on the ground floor of a lobby.

### TIMING

A company has 21 days from the date of service to either make payment of the demand, or file an application to have the statutory demand set aside.

A failure by the company to take either of those steps will result in a presumption that the company is insolvent, which opens the door for the creditor to commence winding up proceedings.

### APPLICATION TO SET ASIDE

A creditor should be aware of the circumstances in which a company may make an application to set aside a statutory demand.

Ultimately, any application to set aside a statutory demand must be filed in the Court and served within 21 days after the statutory demand is served. This strict time period forces the company to move quickly to dispute the statutory demand if it claims the debt is not owing or it has a good reason not to pay it.

The application must be supported by an affidavit which outlines the grounds for contesting the statutory demand. A company cannot file any additional material with fresh grounds for after the 21 day period expires.

The Court can set aside the statutory demand if the Court is satisfied that:

1. THERE IS A GENUINE DISPUTE ABOUT THE EXISTENCE OF, OR AMOUNT, OF THE DEBT. This means the dispute must be real and not spurious, hypothetical or illusory.

This includes, for example, a debtor company's dispute against the validity of a payment claim and their potential entitlement to delay costs issued under a building contract (recently determined in *ABC Constructions No 1 Pty Ltd v Bonelli Constructions Pty Ltd* ).

2. IT HAS AN OFFSETTING CLAIM. A genuine offsetting claim that the company has against the creditor by way of counterclaim, set off or cross demand (even if it does not arise out of the same transaction or circumstances as the debt to which the statutory demand relates).

3. A DEFECT IN THE STATUTORY DEMAND WILL CAUSE SUBSTANTIAL INJUSTICE unless the statutory demand is set aside. A defect can be an irregularity, a misstatement of an amount, or a misdescription of the debt or a person.

4. THERE IS SOME OTHER REASON why the demand should be set aside, including for improper purpose or abuse of process, failing to state (in the supporting affidavit) the source or knowledge, or that the deponent is authorised by the creditor to swear the affidavit and failing to verify that the debt is due and payable.

The Queensland Supreme Court recently determined in *Palmer Petroleum Pty Ltd v BGP Geosplorer Pty Ltd* that the presence of an arbitration clause is not sufficient to form "some other reason".

If the company fails to make an application within the time period, then it cannot later resist an application for winding up on any of the same grounds that it could have relied on to set aside the statutory demand.

### COSTS

If the company is successful in having that statutory demand set aside, then the Court may order the creditor pay the company's cost of the application.

REMEMBER

Prior to issuing the statutory demand, a creditor should consider:

- . whether the sum demanded is in fact a "debt";
- . whether the company has a genuine dispute about the existence of the debt or the amount owing; or
- . whether the company has an offsetting claim.

If the answer to any of those questions is yes, then think twice about issuing a statutory demand and consider other methods of debt recovery.

When issued properly, a statutory demand can be a useful tool in recovering money; but if issued improperly, then there are potential adverse costs consequences for the creditor.

If you have any queries about the issuing, setting aside or resisting an application to set aside a statutory demand, then contact ClarkeKann for assistance or guidance.

FOR MORE INFORMATION, PLEASE CONTACT:



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