Australian Government

Corporations and Markets Advisory Committee

ISSUES IN EXTERNAL ADMINISTRATION

Discussion Paper

February 2008

Corporations and Markets **Advisory Committee**

Issues in external administration

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Request for submissions

The Advisory Committee invites submissions on any aspect of the matters covered in this paper, including the Committee's provisional position on each of the issues in the terms of reference.

Please email your submission, in Word format, to:

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If you have any queries, you can call (02) 9911 2950.

Please forward your submissions by **Friday 16 May 2008**.

All submissions, unless marked confidential, will be published at www.camac.gov.au

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1 Introduction

This chapter explains the background to the reference to the Committee, sets out the terms of reference, outlines the structure of the paper and gives information about the Committee.

1.1 Background to the reference

As part of the review process leading up to the *Corporations Amendment (Insolvency) Act 2007*, the then Government released an Exposure Draft Bill for public consultation.

The Government took into account submissions on the Bill in finalising the amending legislation, effective from 31 December 2007.[1]

However, several matters raised in the submissions were not included in the legislation, and were referred to the Advisory Committee for further consideration.

1.2 Reference to the Advisory Committee

In May 2007, the then Parliamentary Secretary to the Treasurer, the Hon. Chris Pearce, MP (the Parliamentary Secretary), referred to the Advisory Committee for consideration and advice a number of issues related to insolvency law. In his letter, the Parliamentary Secretary said:

> Insolvency law is an important area of the law as it ensures that the capital of insolvent companies is efficiently and equitably redeployed within the economy to be more effectively utilised by other entities. The Corporations Amendment (Insolvency) Bill 2007 will improve Australian insolvency law in a number of areas, in part by implementing recommendations made by the Advisory Committee in previous reports.

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[1] The amending legislation includes reforms recommended by the Corporations and Markets Advisory Committee (the Advisory Committee) in its reports *Corporate Voluntary Administration* (June 1998), *Corporate Groups* (May 2000) and *Rehabilitating large and complex enterprises in financial difficulties* (October 2004).

> A number of new issues were raised by stakeholders during consultation on the content of the Insolvency Bill. Whilst some issues were incorporated into the Bill, there are a number of other issues that would benefit from public discussion and subsequent consideration by the Advisory Committee.

The Parliamentary Secretary requested the Advisory Committee to consider and advise on each of the following proposals, drawn from submissions on the Bill.

Voluntary administration

- The administrator of a company should be required to provide access to a list of a company's known creditors as soon as practicable after their appointment (Issue 1).
- The administrator of a company should be required to provide details of the location of all equipment in the possession of the company owned by entities other than the company. These details might be included in the s 443B(3) notice that informs the owner or lessor that the company does not propose to exercise rights in relation to the property (Issue 2).
- A nominee of an administrator should be allowed to chair the second [major] meeting in voluntary administration, where the administrator is sick or otherwise unable to attend in person (Issue 3).
- The deed administrator should be required to notify creditors of any breach of a deed of company arrangement (Issue 4).
- Directors and related party creditors should be prevented from voting on a proposal to appoint a different person as liquidator when a company proceeds from administration into liquidation (Issue 5).
- Where a company is put into liquidation after an administration (or deed of company arrangement) then the remuneration of the administrator (or deed administrator) should be provided a priority over that of any replacement liquidator (Issue 6).

Liquidation

- Creditors should be able to approve the remuneration of a provisional liquidator when a company proceeds from provisional liquidation into liquidation (Issue 7).

- A new mechanism should be introduced to allow for voting by post on proposals relating to remuneration, compromise of debts under s 477(2A) and liquidators entering into agreements on the company's behalf under s 477(2B) (Issue 8).

- The defences to the voidable transaction provisions should be amended, such that the insolvency defence under section 588FG does not apply to the new provisions relating to transactions entered into while a company was under administration (given that insolvency is not a condition for those provisions) (Issue 9).

- ASIC should be able to apply to a court to replace a liquidator if the liquidator dies or is no longer registered (Issue 10).

- ASIC should be able to take possession of books relating to a company in external administration, and transfer those books to another liquidator, if a liquidator dies or is no longer registered (Issue 11).

Receiverships and other controllerships

- The definition of 'controller' should be revised such that enforcing a security over a single asset, or an asset with a value of less than $100,000, does not involve a controllership and the requirements of the Corporations Act dealing with controllers are not applicable (Issue 12).

- Transactions conducted under the authority of a receiver or controller should be exempted from the voidable transaction provisions (Issue 13).

Communication in external administrations

- The requirement to publish insolvency notices in a newspaper should be limited, such that it requires only a summary statement with additional details to be published on a website to be maintained by ASIC or a professional body. An alternative

proposal would move all notices to a website to be maintained by ASIC or a professional body (Issue 14).

- The rule allowing a deed administrator to apply to the court for an exemption from the rule requiring a company to publish its former name on public documents should be extended to all other types of external administration (Issue 15).

- The new mechanism for electronic communication with creditors should be extended, to allow for electronic means to be used except if the creditor requests a hard copy of documents. One suggested approach would provide for a single page to be sent to creditors directing them to documents available on a website and providing a telephone number to call if a hard copy is required. An alternative proposal would provide for a creditor being ‘deemed’ to have consented to electronic communication where a company has communicated with a creditor by that means at any time prior to the commencement of the external administration (Issue 16).

The reference to the Advisory Committee also requested advice on whether the requirement for a members’ scheme of arrangement to be approved by a majority in number of the members present and voting should be removed. The Advisory Committee will include this matter in a forthcoming discussion paper on members’ schemes of arrangement.

1.3 Outline of the paper

Some key features of the various forms of external administration are summarised in Chapter 2 by way of background.

The issues in the Referred Proposal are discussed as follows:

- voluntary administration (Chapter 3, Issues 1–6)

- liquidation (Chapter 4, Issues 7–11)

- receiverships and other controllerships (Chapter 5, Issues 12–13)

- matters affecting several forms of external administration (Chapter 6, Issues 14–16).

The paper sets out the background to each issue, discusses relevant policy considerations and advances a provisional Advisory Committee position, together with reasons for that position. In indicating its current thinking in this way, the Advisory Committee is seeking to engage respondents in their consideration of the issues and draw out other views or considerations. The Committee emphasises, however, that all the issues remain under consideration and it will not reach a settled position on them until it has considered all submissions on this paper.

1.4 The Advisory Committee

The Advisory Committee is constituted under Part 9 of the *Australian Securities and Investments Commission Act 2001*. Its functions include, on its own initiative or when requested by the Minister, to provide advice to the Minister about corporations and financial services law and practice.

The members of the Advisory Committee are selected by the Minister, following consultation with the States and Territories, in their personal capacity on the basis of their knowledge of, or experience in, business, the administration of companies, financial markets, financial products and financial services, law, economics or accounting.

The current members of the Advisory Committee are:

- Richard St John (Convenor)—Special Counsel, Johnson Winter & Slattery, Melbourne
- Zelinda Bafile—Lawyer, Director and former General Counsel and Company Secretary, Home Building Society Ltd, Perth
- Barbara Bradshaw—Chief Executive Officer, Law Society Northern Territory, Darwin
- Jeremy Cooper—Deputy Chairman of the Australian Securities and Investments Commission
- Alice McCleary—Company Director, Adelaide
- Marian Micalizzi—Chartered Accountant, Brisbane
- Robert Seidler—Partner, Blake Dawson Waldron, Sydney

- Greg Vickery AM—Chairman and Partner, Deacons, Brisbane
- Nerolie Withnall—Company Director, Brisbane.

A Legal Committee has also been constituted to provide expert legal analysis, assessment and advice to the Advisory Committee in relation to such matters as are referred to it by the Advisory Committee.

The members of the Legal Committee are selected by the Minister, following consultation with the States and Territories, in their personal capacity on the basis of their expertise in corporate law.

The current members of the Legal Committee are:

- Nerolie Withnall (Convenor)—Company Director, Brisbane
- Lyn Bennett—Partner, Hunt & Hunt, Darwin
- Elizabeth Boros—Professor of Law, Monash University, Melbourne
- Damian Egan—Partner, Murdoch Clarke, Hobart
- Jennifer Hill—Professor of Law, University of Sydney
- James Marshall—Partner, Blake Dawson Waldron, Sydney
- David Proudman—Partner, Johnson Winter & Slattery, Adelaide
- Laurie Shervington—Partner, Minter Ellison, Perth
- Simon Stretton—South Australian Crown Solicitor, Adelaide
- Gabrielle Upton—Legal Counsel, Australian Institute of Company Directors, Sydney.

The Executive comprises:

- John Kluver—Executive Director
- Vincent Jewell—Deputy Director
- Anne Durie—Legal Officer
- Thaumani Parrino—Office Manager.

2 Forms of external administration

By way of background, this chapter summarises some of the key features of the various forms of external administration.

2.1 Overview

Companies that are or are likely to become insolvent[2] may go into various forms of external administration, either on their own initiative or at the instance of one or more creditors.

Forms of external administration that may be initiated by the company itself are:

- voluntary administration[3]
- creditors' scheme of arrangement[4]
- voluntary winding up.[5]

Forms of external administration that may be initiated by other persons are:

- receivership and other forms of controllership[6]
- winding up by the court.[7]

The effect of entering into a voluntary administration or any form of winding up is that the running of the company passes from the directors to an administrator or a liquidator. The directors retain their formal powers in a creditors' scheme of arrangement or a receivership, though their capacity to run the company may be constrained by the terms of the creditors' scheme or the control exercised by the receiver over the company's assets.

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2 The test of solvency is found in s 95A.
3 Part 5.3A.
4 Part 5.1.
5 Part 5.5.
6 Part 5.2.
7 Parts 5.4, 5.4A, 5.4B.

2.2 External administration initiated by the company

2.2.1 Voluntary administration

An administrator may be appointed to a company that is insolvent or likely to become insolvent. Usually, the company's directors make this decision.[8]

One consequence of a company entering into a voluntary administration is that there is a stay or moratorium on actions or proceedings against the company and its property.

A major task of the administrator is to prepare a report to the company's creditors about the company's affairs.

The creditors have two meetings. The first meeting gives creditors a preliminary opportunity to obtain some information about the state of the company. They can also appoint a committee of creditors and have the power to replace the administrator. At the second (major) meeting, the creditors decide on a future course of action for the company. They may agree to the company returning to active trading, the company restructuring its affairs under a deed of company arrangement (DOCA), or the company being wound up.

Creditors may agree under a DOCA to postpone payment of their debts or to accept less than full payment. A company subject to a DOCA can be run by a deed administrator or by the directors themselves, depending on the terms of the deed.

2.2.2 Creditors' scheme of arrangement

Before the introduction of voluntary administration in 1993, it was common for insolvent companies to restructure their affairs under a creditors' scheme of arrangement. However, this form of external administration has largely been replaced by voluntary administration.

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8 s 436A. An administrator may also be appointed by a substantial chargeholder (s 436C) or by a liquidator or provisional liquidator (s 436B).

2.2.3 Voluntary winding up

A company may choose to go into liquidation by special resolution of its members.[9]

This voluntary form of liquidation is a members' voluntary winding up if the company is solvent and is a creditors' voluntary winding up if the company is insolvent.[10]

2.3 External administration initiated by other persons

2.3.1 Receivership

A company may grant a charge over some or all of its property as security for money lent to it. If the company defaults on the loan agreement, the lender can appoint a receiver or other person to take control of the relevant property and sell it to satisfy the company's debt. Receivers and other persons taking control of a company's property are referred to as 'controllers'.[11]

2.3.2 Court winding up

Where a company is insolvent, one or more of its creditors can apply to the court to have it wound up.[12] A company may also be wound up by court order on various other grounds going beyond insolvency.[13]

It can take some time from the filing of an application for a winding up order for the matter to be determined by the court. The court has a discretion to appoint a provisional liquidator to take control of the company during this interim period.

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9 s 491.

10 The creditors' voluntary winding up provisions are also taken to apply when creditors in a voluntary administration resolve that the company be wound up, when the creditors resolve that the company execute a deed but the company fails to do so within the permitted time or when the creditors of a company subject to a deed of company arrangement resolve to terminate the deed and that the company be wound up (s 446A).

11 s 9 definition of 'controller'.

12 ss 459A, 459P.

13 ss 461–464.

3 Voluntary administration

This chapter considers issues specifically related to voluntary administration, namely those relating to the duties of an administrator, the operation of the deed of company arrangement and winding up following an administration.

3.1 Duties of an administrator

3.1.1 Context

A voluntary administration commences with the appointment of the administrator, usually by the directors of the company.[14]

The administrator must:

- as soon as practicable after the commencement of the administration, investigate the company's business, property, affairs and financial circumstances[15]
- convene the first meeting of the company's creditors, which must be held within 8 business days after the administration begins, with creditors to receive notice at least 5 business days before the meeting[16]
- convene and preside at the second (major) meeting of the company's creditors, which decides the future course of action for the company.[17]

The terms of reference raise three issues relating to these duties, namely whether the administrator should be required to:

- provide access to a list of a company's known creditors (Issue 1)

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14 s 436A. An administrator may also be appointed by a substantial chargeholder (s 436C) or by a liquidator or provisional liquidator (s 436B).

15 s 438A.

16 s 436E.

17 ss 439A–439C.

- provide details of the location of all equipment in the possession of the company owned by entities other than the company (Issue 2)
- chair the major meeting in person (Issue 3).

3.1.2 Issue 1: Access to creditor list

The Referred Proposal is that:

> The administrator of a company should be required to provide access to a list of a company's known creditors as soon as practicable after their appointment.

Background

An administrator may, but is not obliged to, provide access to a list of the company's known creditors following his or her appointment. In the absence of this information, creditors must resort to identifying other creditors at creditors' meetings or obtaining details of those creditors from reports issued by the administrator.

By contrast, in voluntary windings up where the company is insolvent, the liquidator must send to each known creditor, with the notice convening the meeting, a list setting out:

- the names of all known creditors
- the contact details of those creditors, and
- the estimated amounts of their claims.[18]

However, if the debt owed to a creditor is less than $1,000, the liquidator only needs to specify where a copy of that list may be obtained.[19]

Is there a need for any change?

Arguments in favour of retaining the current position are:

- some creditors may be concerned about the disclosure of commercially sensitive financial information to other persons

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18 ss 496(2), 497(2). The Corporations Act allows for these notices to be sent electronically: s 600G.

19 ss 496(3), 497(3).

- the list may encourage proxy hunting by creditors
- any requirement to mail the list may increase administrative costs
- the list could in some circumstances make it easier for other insolvency practitioners to lobby creditors to replace the administrator.

Arguments for making some change to the current position are:

- other creditors may wish to know who else is owed a debt by the company
- it should be made easier for creditors to inform themselves and protect their interests by consulting with each other about the future course of action for the company.[20]

If some change to the current position is considered appropriate, the following questions arise:

- what information concerning creditors should an administrator disclose
- when, and
- to whom.

Policy options on information to be disclosed

The policy options include:

- *Option 1:* administrator to provide a list of the names and contact details of the company's known creditors
- *Option 2:* as in Option 1 and in addition disclose the estimated amounts of creditor claims.

Option 1: Names and contact details only

The advantage of this option is that it would allow for known creditors to be informed about who are their fellow creditors without undue administrative burden or cost (given that the administrator is

[20] The Australian Bankers' Association Submission on the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007 paras 9.4–9.10.

already required to ascertain the identity of the company's creditors prior to the first meeting to give them written notice of the meeting[21]).

Option 2: Names, contact details and amounts

Arguments for the list recording the value of the debt as well as the identity of the creditors are that it would:

- assist creditors to determine whether a resolution is likely to be passed by value as well as by number
- assist creditors to organize sufficient votes to pass a resolution by value as well as by number by identifying the major creditors of a company
- provide known creditors with all the relevant information without placing the onus on them to obtain it.

An argument against disclosing the amount of the debt is that it may damage the general commercial position of some creditors, for instance by drawing attention to the possibility that they may be under financial pressure through lack of payment.[22]

Policy options on timing of disclosure

The policy options include providing the list:

- *Option 1:* as soon as practicable after the appointment of the administrator
- *Option 2:* with the notice of the first meeting of the creditors
- *Option 3:* at the first meeting of the creditors.

Options 1 and 2 would ensure that the information is made available early in the administration when it may be most useful to creditors. Currently, the creditors of a company in administration are often disclosed to the general body of creditors at a subsequent stage, for example in the report that administrators must send to creditors with the notice of the major meeting.[23] Giving creditors early access to

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21 In accordance with s 436E(3).

22 The Australian Bankers' Association, on whose submission the Referred Proposal was based, did not favour disclosure of the amount of debts.

23 s 439A.

the list may assist them if they are considering removing the administrator, a right that can be difficult to exercise if creditors do not know who are the other creditors.

While not requiring disclosure as early as Options 1 and 2, Option 3 would still give creditors the opportunity to consult about the decision to be made subsequently at the major meeting.

Policy options on recipients of information

The policy options include providing the list to:

- *Option 1:* the company's creditors
- *Option 2:* the company's creditors, other than creditors owed less than $1,000
- *Option 3:* the market generally (through, say, publication on the Internet).

The advantages of publishing the list on the Internet are that:

- it would avoid undue administrative cost
- it may help inform the company's creditors of whom the administrator is not aware
- the list could be updated as other creditors emerge.

The principal concerns are whether persons other than creditors should have access to information about a company's creditors, and the possible commercial sensitivity of this information, particularly if it includes the amount of the debts.

Advisory Committee provisional position

> PP1
>
> To assist creditors in their collective decision-making in a voluntary administration, an administrator should publish on a designated website the name, contact details and estimated amount due in relation to each creditor of a company in voluntary administration no later than the time of distribution to creditors of the notice of the first meeting.

The concept of a designated website is discussed at Section 6.1.2.

Reasons

Given the responsibility of creditors in deciding the future course of action for a company in a voluntary administration, it is important that they be provided with timely and complete information to assist them in that process.

Publication on the Internet would be simple to administer and would overcome the costs of mailing information to all known creditors (or all creditors owed more than $1,000).

The Committee does not see proxy hunting as a concern. Proxies can only be given with the consent of persons entitled to vote. It is normal commercial practice for persons to solicit proxies on matters that they consider important.

Issue arising from PP1

Would it be preferable to identify the amount of each claim within designated bands, rather than having to disclose an estimate of the specific amount due?

The use of bands might simplify the disclosure process. In some cases, depending on the width of the bands, it may reduce commercial sensitivity about the disclosure of amounts particular creditors are owed.

3.1.3 Issue 2: Administrator's notice to property owners

The Referred Proposal is that:

> The administrator of a company should be required to provide details of the location of all equipment in the possession of the company owned by entities other than the company. These details might be included in the s 443B(3) notice that informs the owner or lessor that the company does not propose to exercise rights in relation to the property.

Background

Administrators need to consider whether the company will retain any equipment or other property in the company's possession that is owned by a third party.[24]

An administrator who decides not to retain such property may notify the owner of that decision within 5 business days after the commencement of the administration.[25] An administrator who fails to notify the owner becomes personally liable for the company's debts in relation to its use of that property after the end of the 5 business day period,[26] subject to indemnity rights against the company's property.[27]

However, an administrator who exercises the right to avoid liability by notifying an owner is not obliged to disclose in the notice the location of the property.

Implementation of the Referred Proposal

The proponent of this proposal[28] suggests that:

- administrators should be required to detail the location of the property in the relevant notice to the owners, including lessors and financiers
- administrators should ensure that the property is available for quick and easy repossession at the specified location for a set time after service of the notice
- failure by the administrator to ensure that the property is at the location when the owner or financier seeks to recover it within the stipulated time should constitute use of the property and the notice would cease to have effect.

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24 For instance, a person might:
- lease goods to a company or
- own goods used by the company or in the company's possession under a Romalpa clause (which provides that title to goods does not pass from the vendor to the purchaser until they have been paid for).

25 s 443B(3).

26 s 443B(2), (4).

27 s 443D.

28 Australian Finance Conference Submission on the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007, Issue 2.

A possible variation would be to require administrators to give the relevant information only ‘to the best of their knowledge and belief’.

Policy considerations

An argument for the proposal is that it would assist owners of property, without placing an undue additional burden on administrators. Administrators of lessee companies have a strong incentive to identify and locate all leased assets, given that they automatically become liable for payments on those assets after a certain period of time.

Arguments against the proposal are:

- owners of equipment can communicate directly with the administrator to arrange for its recovery
- these owners can negotiate for the original lease contract to include a term requiring disclosure of the location of the equipment.

Advisory Committee provisional position

PP2

An administrator issuing a s 443B notice should be required to disclose in the notice the location of the relevant equipment to the extent that this information is reasonably available to the administrator. In addition, the administrator should have a general obligation to facilitate efforts by owners to locate property that the administrator will not be using.

It is not proposed that there be a specific penalty or other sanction on the administrator for failure to comply with either requirement. Rather, the intent is that ASIC or any other interested party could take judicial proceedings to enforce either requirement.

Reasons

An owner of property should in principle have a right to be informed about the location of that property. Limiting the administrator’s obligation to information that ‘is reasonably available to the administrator’ should minimise the burden on administrators.

3.1.4 Issue 3: Chairing the major meeting of creditors

The Referred Proposal is that:

> A nominee of an administrator should be allowed to chair the second [major] meeting in voluntary administration, where the administrator is sick or otherwise unable to attend in person.

Background

In general, insolvency practitioners may send a nominee in their place to chair meetings of creditors.[29] However, an administrator is required to chair the major meeting of creditors in a voluntary administration.[30] This reflects the importance of that meeting in deciding the future course of action for the company.

While an administrator may apply to the court for an order for someone else to chair the meeting, the question is whether there should be some additional flexibility to cover circumstances where the administrator's attendance may not be practical.

Policy considerations

An argument for maintaining the current position is that requiring court approval before an administrator can appoint a nominee:

- allows the court to assess the merits of doing so in each particular case, and
- may minimise the possibility of the administrator 'cherrypicking' which major meetings to attend.

Arguments for giving an administrator a discretion to appoint a nominee without the need for court approval are:

- administrators have a general duty to act in the best interests of creditors

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[29] Corp Reg 5.6.17(1).

[30] s 439B. This provision overrides the general right of an external administrator under Corp Reg 5.6.17(1) to appoint a nominee (see Corp Reg 5.6.11(3)(c)).

- the process of obtaining court approval may slow down the progress of the administration, given that a creditors' meeting could not proceed under a nominee without court approval.

In any move to allow more flexibility, the interests of creditors could be protected by:

- allowing a substitute chair only where an administrator is unable to attend the major meeting of creditors because of illness or some other good reason[31]
- requiring that the nominee be a registered liquidator
- requiring that the nominee be approved by a resolution of creditors, with the administrator providing to creditors before the vote is taken details of the nominee's experience and knowledge of the administration, including a statement that the nominee is 'in a position to answer questions'[32] about the administration
- requiring that the meeting be automatically adjourned for a set period if the creditors do not approve the nominee, to give the administrator the opportunity to be present at the adjourned meeting or to make an application to the court to approve the use of a nominee.

Advisory Committee provisional position

PP3

The general expectation should be that the administrator will chair the major meeting of creditors, given that it decides the future course of action for the company. However, an administrator should have a discretion to nominate another person to chair the major meeting of creditors where:

- the administrator cannot attend that meeting because of illness or some other good reason, and

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31 Compare ss 588H and 588FGB, which provide directors with a defence to actions for insolvent trading and to proceedings for certain orders to indemnify the Commissioner of Taxation, respectively. Under those provisions, a 'good reason' does not include duress or undue influence: *Deputy Commissioner of Taxation v Clark* (2003) 45 ACSR 332 at 359–365.

32 This would be analogous to the requirements under s 250RA concerning an auditor's representative at a company's annual general meeting.

- the creditors have resolved that the nominee should chair the meeting.

The administrator should be required to provide to the meeting a statement of the reason for his or her inability to attend.

Any nominee should be a registered liquidator. Also, before creditors vote on whether the nominee should chair the meeting, the administrator should:

- disclose relevant information concerning the nominee's experience and knowledge of the administration, and
- certify to creditors that the nominee is in a position to answer questions about the administration.

The meeting should be automatically adjourned for a short period (no more than a week) if the creditors do not approve the nominee presiding.

Reasons

It is desirable to provide administrators with some flexibility, short of a court application, without enabling them to send a nominee to the major meeting merely for reasons of convenience. The interests of creditors would be protected by the requirement that they be provided with relevant information before deciding whether to agree to the nominee.

The Advisory Committee's provisional position would give due weight to the importance of the administrator participating in the major meeting of creditors, while recognising that, in some circumstances, it may be impractical for that to happen.

3.2 Deed of company arrangement

3.2.1 Context

One of the options open to creditors at their major meeting is to approve the company entering into a deed of company arrangement (DOCA).

DOCAs normally take the form of either a moratorium deed (under which the company is permitted a period of time to pay its creditors), a compromise deed (under which creditors agree to accept

a payment less than their full debt as a final settlement) or a combined moratorium and compromise deed.

A DOCA binds all unsecured creditors of the company, as well as any secured creditors and owners or lessors of property who voted in favour of it.[33] The court may also order that other secured creditors and owners or lessors of property be bound by the deed where:

- enforcement of their rights would materially adversely affect the arrangement, and
- their interests are otherwise adequately protected.[34]

Creditors bound by a DOCA may not take action against the company or its property without the leave of the court.[35] Also, they cannot make or proceed with an application for a winding up order.[36]

The creditors of a company subject to a DOCA may only pass a resolution terminating the deed if:

- there has been a breach of the deed, and
- the breach has not been rectified before the resolution is passed.[37]

3.2.2 Issue 4: Notification of breach of deed of company arrangement

The Referred Proposal is that:

> The deed administrator should be required to notify creditors of any breach of a deed of company arrangement.

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33 s 444D(1), (2)(a), (3)(a).

34 ss 444D(2)(b), (3)(b), 444F.

35 s 444E(3).

36 s 444E(2).

37 ss 445C(b), 445CA. The resolution must be passed at a meeting convened under s 445F by a notice setting out the proposed resolution.
The requirement that the breach has not been rectified adopts a recommendation of the Advisory Committee to overcome the possibility that some creditors may require an administrator to convene a meeting to terminate the deed even where the company was complying with its terms: *Corporate voluntary administration* (June 1998) rec 35.
A deed also terminates where the court so orders, on application by a creditor of the company, the company itself, ASIC or any other interested person (s 445D) or where there exist circumstances in which the deed specifies that it is to terminate (s 445C(c)).

Background

There is no statutory requirement for the deed administrator or the directors (if in control of the company under the deed) to inform creditors that a breach of the deed has occurred.

Policy options

Option 1: Obligation to notify all breaches

An argument for a full disclosure obligation is that creditors should be informed of all breaches of the DOCA, given their statutory right to terminate it. Notification will enable them to consider whether to call a meeting, or apply to the court, to terminate the DOCA.

On the other hand, obliging a deed administrator or directors to notify all breaches may impose an undue administrative burden, particularly if it is likely that a breach will be rectified. One possibility is to limit any obligation to notify creditors to circumstances where a breach has not been rectified within a certain period after coming to the notice of the administrator or directors.

Option 2: Discretion whether to notify breaches

An alternative approach is to try to protect creditors without imposing an undue administrative burden by giving a deed administrator or the directors a more general discretion whether to notify creditors of a breach. Deed administrators or directors could be required to notify creditors of any information regarding a breach, or a combination of breaches, that could reasonably be expected to have a material effect on the purpose or outcome of the DOCA. Under this approach, the deed administrator or the directors would not have to notify creditors, for instance, where they considered, in good faith and on reasonable grounds, that the company would benefit from giving a party in breach a period of grace to comply.

Advisory Committee provisional position

PP4

The deed administrator or the directors (if in control of the company under the deed) should be required to notify creditors of any information regarding a breach, or a combination of breaches, that could reasonably be expected to have a material effect on the purpose or outcome of the deed.

Reasons

A requirement to notify creditors of each breach of a deed could be unduly burdensome. It would not take into account commercial practice and could result in creditors becoming unduly involved in the day to day operation of the deed. PP4 would provide greater flexibility, so that creditors would only receive information about breaches that are material and ongoing. A general discretion may be preferable to an obligation to notify creditors where a breach has not been rectified within a certain timeframe, which could have arbitrary effects.

3.3 Winding up following an administration

3.3.1 Context

A company under administration goes into liquidation if:

- the creditors resolve at the major meeting that the company be wound up,[38] or
- the creditors resolve that the company execute a DOCA and the company fails to do so within 15 business days after the end of the meeting of creditors.[39]

A company that is subject to a DOCA goes into winding up if:

- the company's creditors resolve to terminate the DOCA, and that the company be wound up[40]
- the court makes an order terminating the DOCA[41]
- the DOCA specifies circumstances in which it is to terminate and the company be wound up and those circumstances exist.[42]

Where a company under administration or subject to a DOCA goes into winding up, the administrator or deed administrator becomes the liquidator, unless the creditors choose another person.[43]

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38 ss 439C(c), 446A(1)(a), (2).
39 ss 444B(2), 446A(1)(b), (2).
40 ss 445E, 445F, 446A(1)(c), (2).
41 s 445D, Corp Reg 5.3A.07(1)(a)).
42 Corp Reg 5.3A.07(1)(b).

The terms of reference raise two issues where an administrator or deed administrator is replaced by a different person as liquidator, namely:

- whether directors and related party creditors should be permitted to vote on the resolution to appoint a different person as liquidator (Issue 5)
- whether the remuneration of the administrator or deed administrator should have priority over that of the replacement liquidator (Issue 6).

3.3.2 Issue 5: Appointment of new person as liquidator

The Referred Proposal is that:

> Directors and related party creditors should be prevented from voting on a proposal to appoint a different person as liquidator when a company proceeds from administration into liquidation.

Background

The Referred Proposal arises from a concern that certain creditors (referred to in this paper as 'affected creditors'), being:

- those directors who are creditors of a company, or
- any other creditor who is a related party of a director (whether or not that director is also a creditor)

may seek to replace the administrator with a different person as liquidator because the administrator has proposed that the company pursue a recovery action against the directors.

Under the current law, all creditors, including affected creditors, can vote on the resolution to replace the administrator. However, any creditor can apply to the court to have a resolution determined by the

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[43] s 499(2A), (2B), (2C). The right of creditors to choose another person, introduced by the *Corporations Amendment (Insolvency) Act 2007*, adopts the Advisory Committee report *Corporate voluntary administration* (June 1998) rec 54, Parliamentary Joint Committee on Corporations and Financial Services, *Corporate Insolvency Laws: a Stocktake* (June 2004) rec 2.

vote of related creditors set aside on various grounds relating to the overall interests of creditors.[44]

The Referred Proposal would go further by excluding affected creditors from voting on this type of resolution.

Policy options

Possible policy options include:

- *Option 1:* no change
- *Option 2:* prohibit affected creditors from voting on a resolution to choose a different person as liquidator
- *Option 3:* give the former administrator a right of appeal.

Option 1: No change

Under this option, there would continue to be no restrictions on voting by creditors. However, any creditor who is concerned that affected creditors were voting for an improper purpose would retain the right to request the court to overturn the resolution.[45]

Option 2: General prohibition on voting

This option would effectively deny all affected creditors the right to vote on a replacement resolution, to avoid the possibility of improper voting.

The proponent of the proposal[46] identified competing policy considerations in assessing this option:

- on the one hand, creditors should have the right to choose a different person as liquidator if they consider that the administrator is performing poorly or there is a genuine or perceived lack of independence
- on the other hand, an administrator should not be threatened with replacement for the wrong reasons, such as pressure from directors and related party creditors to prevent close examination of matters that may constitute breaches of fiduciary duty,

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[44] s 600A.
[45] ibid.
[46] Insolvency Practitioners Association Submission on the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007 para 10.1.1.

insolvent trading, uncommercial transactions or preferences in which those creditors may have been involved.

An argument for Option 2 is that, as the directors will usually be the ones to appoint the administrator at the commencement of a voluntary administration, a subsequent decision by them to support a resolution replacing their appointee when the company goes into liquidation may raise a reasonable suspicion that the administrator is threatening their interests.

Arguments against this option include:

- voting rights should not be removed from an entire class of creditors merely on the assumption that some of them may exercise their vote for an improper purpose
- creditors have an economic interest in the company and particular creditors should not lose their right to participate in any decision to choose a different person as liquidator merely because they have a relationship that in fact may be irrelevant to their decision
- it is inappropriate to prevent affected creditors from voting when other creditors may also have conflicts of interest, yet not be affected by the prohibition
- it is inappropriate to draw an analogy with the general exclusion of voting rights in related party transactions, given that those restrictions apply only to proposed commercial transactions between a company and particular persons
- any liquidator, whether the original administrator or a replacement liquidator, has a duty to pursue actions against the company's officers where appropriate and may be subject to disciplinary action by the Companies Auditors and Liquidators Disciplinary Board for improper failure to do so.

A modified version of Option 2 to take these concerns into account might be:

- to exclude from voting on the resolution to choose a new person as liquidator any creditor against whom the administrator has recommended that an action be taken, but
- give excluded persons a right to apply to the court for an order that they be permitted to vote.

An argument against this modified version of Option 2 is that in practice reports by administrators[47] that refer to possible litigation being commenced tend not to identify particular individuals.

Option 3: Right of appeal by administrator

An administrator who has been replaced when the company goes into liquidation as a result of a vote by creditors could be given the right to apply to the court to overturn the decision on the basis that certain parties who voted for removal have abused their voting rights. A removed administrator would be personally liable for the cost of any application to overturn the resolution for removal, in the absence of a court order to the contrary.

Advisory Committee provisional position

PP5

There should be no change to the current position under which all creditors, including creditors who are directors or related parties of those directors, have the right to vote on a resolution to appoint a different person as liquidator when a company proceeds from administration into liquidation.

Reasons

It would be inappropriate to single out a class of persons for exclusion from voting on the basis that one or more members of that class might in a particular circumstance exercise their vote for an improper purpose. Replacement liquidators have an incentive to consider whether to pursue any actions identified in the administrator's report, given that they are subject to the disciplinary jurisdiction of the Companies Auditors and Liquidators Disciplinary Board.

Issues arising from PP5

Should anyone, in addition to a creditor, have a right to challenge a resolution appointing a new person as liquidator? If so, what type of remedy should be available?

[47] s 439A.

3.3.3 Issue 6: Administrator's remuneration

The Referred Proposal is that:

> Where a company is put into liquidation after an administration (or deed of company arrangement) then the remuneration of the administrator (or deed administrator) should be provided a priority over that of any replacement liquidator.

Background

Insolvency practitioners conducting the external administration of a company receive remuneration from the assets of the company for their work. Their right to this remuneration is protected by certain lien and priority rights.

It is common in practice for incoming liquidators to reach an agreement with former administrators about the payment of their respective remuneration out of available corporate assets. However, where agreement cannot be reached, the question becomes how best to balance the right to any unpaid remuneration of an administrator or deed administrator of a company and the similar right of any other person who subsequently becomes the liquidator of the company.

Any remuneration of an administrator or a liquidator must:

- be reasonable,[48] and
- be approved by creditors or the court.[49]

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[48] ss 449E(4) (administrator, deed administrator), 473(10), 499(6), (7), 504(2) (liquidator).
The Insolvency Practitioners Association *Code of Professional Practice for Insolvency Professionals* also contains guidelines for determining remuneration.

[49] ss 449E(1) (administrator), 449E(1A) (deed administrator), 473(3), 499(3), (3A) (liquidator). This procedure was adopted for administrators and deed administrators pursuant to Advisory Committee recommendations: *Corporate voluntary administration* (June 1998) rec 38, *Rehabilitating large and complex enterprises in financial difficulties* (October 2004) rec 18.
Where the decision rests with the creditors or the committee of creditors or the committee of inspection, administrators, deed administrators and liquidators must provide the relevant persons with a report setting out:
- such matters as will enable them to make an informed assessment about whether the proposed remuneration is reasonable
- a summary description of the major tasks performed, or likely to be performed, by the administrator, and

While administrators are in charge of a company, they have an indemnity out of the assets of the company, and a lien to support that indemnity, to cover their remuneration rights.[50] The lien remains in force even after the assets under the administrator's control pass to any subsequent liquidator. However, from a practical point of view, it is easier for an administrator to enforce the lien by deducting from available cash of the company a sufficient amount to cover his or her remuneration before transferring that cash to the control of the liquidator. Also, the lien rights of administrators do not extend to corporate assets recovered after their replacement.

Where remuneration is still owing to administrators at the time of their replacement, they can rely on their general priority right as external administrators, as against other unsecured creditors, for payment out of the company's assets on a liquidation.[51] However, that priority right only ranks equally with a similar right of the liquidator.[52]

- the costs associated with each of those major tasks (ss 449E(5), (6), (7) (administrators and deed administrators), 473(11), (12), 499(6), (7) (liquidators)).

There is provision for court review of the remuneration of administrators and deed administrators (s 449E(2)) and liquidators (s 504).

50 The administrator of a company is entitled to be indemnified out of the company's property for his or her remuneration (s 443D(b)). This right of indemnity:

- has priority over the company's unsecured debts, as well as priority over debts secured by a floating charge where the chargee has not taken enforcement action before the commencement of the administration and the remuneration accrues before the administrator receives any notice of an enforcement action taken by the chargee after the commencement of the administration (s 443E)
- is secured by a lien on the company's property (s 443F), and
- is said to be 'subject to section 556' (s 443E(1)).

The Advisory Committee's *Corporate voluntary administration* report (June 1998) made the following comment on the relationship between the lien referred to in s 443F and the priority payments in a liquidation (s 556):

> the administrator's lien would not extend to property gathered in by a liquidator in a winding up, including unfair preferences. If the property subject to the administrator's lien proves insufficient to meet the full amount of the remuneration, and the administrator must rely on property gathered in by the liquidator, the administrator would have a deferred priority for the shortfall (para 6.38).

51 Under the provision providing for priorities in a winding up, the remuneration of external administrators is a priority payment, ranking ahead of ordinary unsecured creditors (s 556).

52 The administrator's remuneration is a 'deferred expense' and, as such, ranks below various other costs of an external administration (s 556(1)(de), definition of 'deferred expenses' in s 556(2)). This deferred priority for remuneration does not distinguish between the different types of insolvency practitioners involved in a particular external administration, all of whom rank equally among themselves.

The effect of the Referred Proposal would be to give any remuneration of the administrator that is outstanding at the time of appointment of another person as the liquidator a higher priority than the liquidator's remuneration.

Policy considerations

Arguments for the Referred Proposal are that it would:

- create certainty between the administrator and any replacement liquidator. An incoming liquidator would be aware of the administrator's remuneration priority and could take that into account in managing the liquidation process
- reduce the possibility of administrators intentionally converting company property into cash to ensure that they can immediately draw on that cash to cover any unpaid remuneration should they be replaced
- reduce the reluctance of some administrators to continue trading on behalf of the company, given that the company may only receive payments from trading in the longer term, after they have been replaced. Their lien rights do not extend to these later-recovered receivables.

Also, the administrator's lien may not always be of value. For instance, there will be no assets under the control of, and therefore available to, an administrator where a receiver is appointed at the same time under a fixed and floating charge over the whole of the company's property.

An argument against the Referred Proposal is that it may discourage potential liquidators from undertaking that role, as they may anticipate a reduced likelihood of being paid.

Advisory Committee provisional position

PP6

Where a company is put into liquidation after an administration (or deed of company arrangement), the remuneration of the administrator (or deed administrator) should have priority over that of any replacement liquidator.

Reasons

Administrators or deed administrators who have already performed functions for the company should have greater certainty that they will be paid for work done in carrying out the duties of their office. The proposed priority would achieve this.

The possibility that PP6 may act as a disincentive for a potential liquidator to accept the appointment is outweighed by the benefit of certainty for administrators, which could encourage them to focus more on trying to save the company.

3.4 Request for submissions

The Advisory Committee invites comments on any aspect of the matters raised in this chapter, including the Advisory Committee provisional positions on Issues 1 to 6 and the related issues.

4 Liquidation

This chapter considers issues specifically related to liquidation, namely the role of creditors, defences to the voidable transaction provisions and the role of the regulator.

4.1 Role of creditors

4.1.1 Context

Creditors have a more limited role in a winding up than in a voluntary administration, given that the company's future course of action is settled by the company going into liquidation.

The terms of reference raise two issues affecting creditors, namely whether:

- they should be able to approve the remuneration of a provisional liquidator when a company proceeds from provisional liquidation into liquidation (Issue 7)
- they should be able to vote by post on specified matters (Issue 8).

4.1.2 Issue 7: Provisional liquidator's remuneration

The Referred Proposal is that:

> Creditors should be able to approve the remuneration of a provisional liquidator when a company proceeds from provisional liquidation into liquidation.

Background

There can be some time between the filing of an application for a winding up order and its determination by the court. The court has a discretion to appoint a provisional liquidator to take control of the

company during this interim period.[53] The provisional liquidator has various powers, including to carry on the business of the company.[54]

The remuneration of a provisional liquidator can only be determined by the court.[55]

By contrast, creditors can approve the remuneration of a court-appointed liquidator, with the court determining this matter if the creditors fail to do so.[56] In making any decision on remuneration, creditors must be provided with a report by the liquidator setting out:

- a summary description of the major tasks performed, or likely to be performed, by the liquidator
- the costs associated with each of those major tasks, and
- such other matters as will enable creditors to make an informed assessment about whether the proposed remuneration is reasonable.[57]

Policy considerations

Arguments in favour of the Referred Proposal are:

- the creditors, as key interested parties when a company is in liquidation, are the appropriate persons from whom provisional liquidators should seek the approval of their remuneration[58]
- judges may not be best qualified to work out remuneration.[59]

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53 s 472(2).

54 s 472(3), (4), (6).

55 s 473(2).

56 s 473(3). See also *Re Interchase Corporation Limited (in provisional liquidation)* (1993) 11 ACLC 849, *Re WA Pines Pty Ltd (in liq)* (1994) 12 ACLC 328. The court's assistance should not be sought merely because the determination is difficult or inexpedient: *Re Molyneux Aluminium Pty Ltd* [1970] VR 456, *Re Sectam Pty Ltd* (1990) 8 ACLC 476.
The court also has certain powers to confirm, increase or reduce remuneration decided by agreement between the liquidator and the committee of inspection or by resolution of creditors: s 473(5), (6).

57 s 473(11), (12).

58 Insolvency Practitioners Association Submission on the Exposure Draft of the Insolvency Bill para 20.2.

59 In *Re DS Millard & Son Pty Ltd* (1997) 15 ACLC 808, a matter dealing with the determination of the remuneration of a liquidator, not a provisional liquidator, Young J stated:

Creditors determining the remuneration of a provisional liquidator could be given the same type of information as that provided to creditors by a liquidator.

Arguably, any new power for creditors to determine the remuneration of a provisional liquidator should not exclude the court's current power to do so.

Advisory Committee provisional position

PP7

Creditors, in addition to the court, should have the power to approve the remuneration of a provisional liquidator when a company proceeds from provisional liquidation into liquidation. To assist them in making this decision, creditors should be given similar information to that provided to creditors in other forms of external administration.

The court should have the power to confirm, increase or reduce the remuneration determined by the creditors.

Reason

Creditors should have the same rights in relation to determining remuneration, whether the person in control of the company is a liquidator or a provisional liquidator.

4.1.3 Issue 8: Postal voting by creditors

The Referred Proposal is that:

> A new mechanism should be introduced to allow for voting by post on proposals relating to remuneration [of a liquidator], compromise of debts under s 477(2A) of the *Corporations Act 2001* (Corporations Act) and liquidators entering into agreements on the company's behalf under s 477(2B) of the Corporations Act.

Judges are not really qualified to work out remuneration. If a judge is asked to do so, it may well be that, in the normal course, he will either refer it to the Registrar for advice or get independent evidence as to the reasonableness of the remuneration.

Background

Specified matters

The Referred Proposal specifies three matters:

- remuneration of liquidators
- compromise of debts
- long-term agreements.

Remuneration of liquidators. Determining the remuneration of a liquidator is in the first instance a matter for agreement between the liquidator and the creditors' committee of inspection.[60] However, if there is no committee of inspection, or the liquidator and the committee cannot agree, the matter may be determined by a resolution of creditors, passed at a meeting convened by the liquidator, or by the court in the absence of a creditors' resolution.[61] The court may also review any remuneration set by the committee of inspection or by the meeting of creditors, on the application of various parties.[62]

A liquidator who convenes a meeting of creditors for the purpose of determining remuneration must attach to the notice of meeting a statement of all receipts and expenditure by the liquidator and the amount of remuneration sought by him or her.[63]

Compromise of debts. A liquidator cannot compromise a debt of more than $100,000 owing to the company, without the approval of the court, the committee of inspection or a resolution of creditors.[64] A liquidator may unilaterally compromise a lesser amount claimed by the company.

Long-term agreements. A liquidator cannot enter into any long-term agreement, such as a lease or a charge, without the approval of the

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60 s 473(3)(a).
61 s 473(3)(b).
62 ss 473(5), (6).
63 s 473(4).
64 s 477(2A), Corp Reg 5.4.02. Contrast the Insolvency Service (UK), *Consultation Paper* (September 2007), which proposes abolition of the requirement for creditor approval of a compromise of a debt or claim, with this matter being left to the commercial judgment of the liquidator (Proposal 2).

court, the committee of inspection or a resolution of creditors.[65] The need to enter into long-term agreements is most likely to arise where the winding up will take an extended time to complete.

Common features

The proposal would permit a liquidator to conduct a postal vote in lieu of a physical meeting for resolutions of creditors concerning any of the specified matters.[66] As already indicated, these matters will usually be considered by the committee of inspection (generally constituted in larger administrations), rather than be voted on by the general body of creditors. Therefore, the question of a postal vote would only arise in limited circumstances.

The proposal does not affect the principles regarding the disclosure of information to creditors, the majority requirements for a creditors' resolution, or the rules concerning the casting vote of a liquidator (including the requirement to give reasons for the exercise of a casting vote). These requirements would be the same for a postal ballot as for a physical meeting.

Consideration of the proposal

Arguments for postal voting

It is arguable that postal voting:

- may increase the efficiency of decision-making in a liquidation by saving the time and expense of a physical meeting of creditors

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[65] s 477(2B). A long-term agreement is one where the term of the agreement may end or the obligations of a party to the agreement may be discharged by performance more than three months after the agreement is entered into, even if it is possible for the term to end or for the obligations to be discharged within those three months.

[66] A precedent is s 64ZBA of the *Bankruptcy Act 1966*, which permits voting otherwise than through a physical meeting.
Compare the approach in The Insolvency Service (UK), *Consultation Paper* (September 2007), Proposal 1, to allow creditors to participate in meetings other than by being physically present:

> For example, the business of the meeting could be conducted with creditors present in person or on the telephone. It would be immaterial whether all those attending the meeting were in the same place. A person would be held to be attending the meeting provided that they could interact and vote at the meeting in such a way that their views could be communicated to all those attending the meeting and their vote could be recorded at the meeting at the same time as votes of others attending the meeting.

- may provide an alternative for creditors who wish to vote but prefer not to appoint a proxy
- overcomes the problem in longer drawn-out liquidations of creditors losing motivation to attend meetings, particularly on more technical procedural issues, such as those related to compromises of debts or long-term agreements, that may arise during the latter stage of a liquidation. A more representative indication of the creditors' wishes might be achieved where creditors have an opportunity to vote by post rather than have to attend a meeting or vote by proxy. Requiring that all matters be determined by a physical meeting may result in a small group of activist creditors dominating these procedural meetings.

Arguments against postal voting

It is arguable that:

- physical meetings can provide a better forum for debate on proposed resolutions, as well as an opportunity for creditors to question the liquidator directly[67]
- particularly in relation to a liquidator's remuneration, there is the potential for a conflict of interest, in that liquidators may seek to have a postal vote to avoid the possibility of creditors discussing the issue, and questioning the liquidator, at a physical meeting
- conversely, creditors in a postal ballot may reject a proposal, without the liquidator having the opportunity to put the case to the meeting (with a liquidator's only option being to request the court to overturn the vote).

Creditor objection

Some creditors may prefer a physical meeting, to allow creditors and the liquidator to discuss the proposal before any vote is taken.

Possible policy options to take into account any objection by creditors to dispensing with a physical meeting include:

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[67] Compare the arguments for retaining physical meetings for listed public companies in the Advisory Committee report *Shareholder Participation in the Modern Listed Public Company* (June 2000), paras 4.142–4.143.

- requiring a physical meeting where a threshold objection level is reached, say, where 5% by number or value of creditors indicate a preference for a physical meeting

- requiring the liquidator to go to court for an order permitting a postal vote where a threshold objection level is reached. The costs of a court application may be less than the administrative costs of running numerous meetings over a long-running liquidation

- giving any creditor, where the threshold objection level is reached, the right to challenge in court a liquidator's decision to conduct a postal vote. The onus could be on the liquidator to establish the grounds for his or her opinion that a postal vote would be reasonable in the circumstances, having regard to the cost of holding the meeting and the nature and content of the proposed resolution.

Advisory Committee provisional position

PP8

A liquidator should have the option to conduct a postal vote on a proposal relating to remuneration, compromise of debts under s 477(2A) and agreements under s 477(2B), with a requirement that a physical meeting be held if a threshold objection level to a postal vote is reached (say, 5% by number or value of creditors).

Reasons

Liquidators should have the ability to conduct a postal vote in some specified circumstances as a means of reducing costs and assisting the administrative process.

The Advisory Committee notes the concern that a liquidator may employ a postal ballot to avoid creditors having the opportunity to meet and discuss matters such as the compromise of a large debt owed to the company or the liquidator's remuneration. However, a liquidator would not necessarily benefit from choosing to conduct a postal ballot, given that creditors may lodge postal votes against the proposed remuneration without the liquidator having the opportunity to deal with creditor concerns or objections at a physical meeting.

Issues arising from PP8

- Should postal voting, if introduced, be permitted beyond the three matters set out in the Referred Proposal?
- Should electronic voting be permitted in addition to postal voting?[68]

If electronic as well as postal voting is permitted, the first vote received by the company should be the one recorded.[69]

4.2 Voidable transactions

4.2.1 Context

Purpose

The voidable transaction provisions seek to protect the interests of the unsecured creditors of an insolvent company that is being wound up. The court is given various powers to set aside particular transactions that were entered into by the company before the winding up began and that may give counterparties or beneficiaries of those transactions an undue advantage over other creditors in the distribution of available corporate assets.

Affected transactions

Voidable transactions are:

- unfair preferences[70]
- uncommercial transactions[71]

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68 The Advisory Committee report *Shareholder Participation in the Modern Listed Public Company* (June 2000) supported the principle of electronic voting, with some qualifications to ensure the integrity of these votes. The report envisaged that electronic voting might be used for voting at shareholder meetings, but foresaw problems in verifying the identity of the persons using that form of voting (para 4.133). It therefore recommended that the Corporations Act should permit the directors of a listed public company to provide for direct absentee voting, subject to any restriction in the company's constitution (rec 20). However, it did not favour absentee voting replacing physical meetings for listed public companies (rec 23).

69 id at para 4.135 and rec 20.

70 Unfair preferences are transactions that result in an entity receiving from the company more than the entity would receive if the transaction were set aside and it were to prove for the debt in a winding up: s 588FA.

- unreasonable director-related transactions[72]
- transactions obstructing creditors' rights[73]
- unfair loans to the company[74]

that were entered into on behalf of the company, before the winding up began,[75] by various parties including:

- directors or officers of the company prior to any voluntary administration (where the company goes from voluntary administration into liquidation)
- (from 31 December 2007) directors or officers of the company pursuant to a DOCA under which the company has been returned to the control of directors (officer-initiated transactions)[76]
- a receiver or other controller (or a person acting under their authority).

However, any transactions entered into by a liquidator or controller on behalf of the company once a winding up begins are not subject to the voidable transaction provisions.[77] Also, transactions entered

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71 Uncommercial transactions are transactions that a reasonable person in the company's circumstances would not have entered into with a counterparty, having regard to various matters, including the benefits and detriment to the company: s 588FB.

72 Unreasonable director-related transactions are transactions with a director or a 'close associate' (defined in s 9) of a director that a reasonable person in the company's circumstances would not have entered into, having regard to various matters, including the benefits and detriment to the company: s 588FDA.

73 Transactions obstructing creditors' rights are transactions at least one of whose purposes is to defeat, delay, or interfere with, the rights of any or all of the company's creditors: s 588FE(5).

74 Unfair loans are loans to the company involving extortionate interest or charges: s 588FD.

75 There are differences between these transactions in relation to the period before the winding up began (or, in some instances, before the relation-back day) in which they must have occurred for them to be voidable: s 588FE.

76 s 588FE(2B), introduced by the *Corporations Amendment (Insolvency) Act 2007*. For the background to these provisions, see the Advisory Committee's report, *Corporate voluntary administration* (June 1998), paras 8.1–8.18, rec 51.

77 This is the effect of s 588FE. A receiver has various powers to carry on a corporation's business during a liquidation: s 420C.

into at any time by an administrator, deed administrator or other person acting under the authority of an administrator or deed administrator are not subject to the voidable transaction provisions.[78]

Action to set aside affected transactions

Where the voidable transaction provisions apply, the liquidator may commence an action against a counterparty or beneficiary of that transaction to undo it. The court has the power to undo voidable transactions, for instance by ordering a counterparty or beneficiary to:

- repay to the company money that the person has received under the transaction, or
- return to the company property received under the transaction.[79]

In most instances, a defendant in these proceedings will have an assumed solvency defence, to the effect that there were no reasonable grounds to suspect at the time of the transaction that the company was insolvent.[80]

Issues

The terms of reference raise two issues concerning voidable transactions, namely whether:

- transactions conducted by a receiver or other controller (or under their authority) should be exempt from the voidable transaction provisions. This is further considered in Section 5.3.2
- the assumed solvency defence should be removed for officer-initiated transactions (Issue 9).

Also, transactions by receivers are not subject to the void dispositions provision in s 468 (which applies to dispositions after the commencement of the winding up), given that the company no longer has a beneficial interest in the relevant property: A Keay, *McPherson: The Law of Company Liquidation* (4th edn, LBC Information Services, 1999) at 225. Presumably the same law would apply to transactions by other controllers.

[78] s 588FE(2A), (2B).

[79] s 588FF.

[80] Under the assumed solvency defence, a beneficiary need only prove there were no reasonable grounds to suspect that the company was insolvent (s 588FG(1)). However, counterparties must also prove that they provided valuable consideration (s 588FG(2)).
The defence is not available for a counterparty in relation to unreasonable director-related transactions or unfair loans: s 588FG(2).

4.2.2 Issue 9: Assumed solvency defence for officer-initiated transactions

The Referred Proposal is that:

> The defences to the voidable transaction provisions should be amended, such that the insolvency defence [that is, the assumed solvency defence] under s 588FG does not apply to the new provisions relating to transactions entered into while a company was under administration (given that insolvency is not a condition for those provisions).

Background

Given the summary of the law in Section 4.2.1, the Referred Proposal to remove the assumed solvency defence would not apply to companies under administration, but would only apply where a company has entered into officer-initiated transactions under a DOCA and has subsequently gone into liquidation. The proposal does not seek to remove that defence for transactions entered into by the company through its directors or other officers before it went into voluntary administration.

Policy considerations

An argument for abolishing the assumed solvency defence for officer-initiated transactions under a DOCA is that removal of the defence would make it easier for the liquidator of a company that goes from a DOCA into liquidation to obtain a court order against the counterparties to unwind the transactions, thereby making more funds available for distribution to the general creditors. The counterparties would share in this distribution, but would receive the same portion of their debt as the other creditors, rather than retaining the full amount, as would be the case where they could successfully rely on the defence.

Arguments for retaining the assumed solvency defence for officer-initiated transactions under a DOCA are:

- the defence protects the interests of bona fide counterparties or beneficiaries in relation to transactions entered into with officers acting on behalf of the company during the DOCA period
- removing the defence may make it more difficult during the DOCA period for officers to enter into transactions on behalf of a company that are designed to assist the company’s recovery,

given that counterparties may be more reluctant to trade with the company if the transaction could be avoided

- it may be too harsh to remove the defence where the counterparty reasonably believes that the company is solvent, but that turns out not to be the case for reasons that the counterparty could not reasonably have foreseen.

Advisory Committee provisional position

PP9

The assumed solvency defence should remain for transactions entered into by officers of a company while a company is under a deed of company arrangement.

Reasons

An amendment to remove the assumed solvency defence would make transactions entered into by directors or other officers under a DOCA too uncertain for the counterparty. Abolition of the defence could undermine corporate rescue plans.

4.3 Role of ASIC

4.3.1 Context

ASIC has a range of functions under the liquidation provisions, including:

- to apply to the court for a company to be wound up[81]
- to apply to the court for authorisation to search for and seize property or books of a company[82] or to examine company officers[83]
- to inquire into the conduct of liquidators[84]
- to cause the accounts of a liquidator to be audited[85]

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81 ss 459P(1)(f), 461–464.
82 s 530C.
83 ss 596A, 596B, para (a) of the s 9 definition of ‘eligible applicant’.
84 s 536.
85 s 539.

- to investigate matters referred to in the reports of liquidators[86]
- to initiate proceedings against anyone in breach of the Corporations Act.[87]

In addition:

- applicants for winding up must lodge a notice of the application with ASIC[88]
- a liquidator must lodge with ASIC a preliminary report about the affairs of the company,[89] as well as a report if it appears to the liquidator that past or present officers, employees or members have committed any offences.[90]

The terms of reference raise whether ASIC should have additional statutory powers to:

- apply to the court for a replacement liquidator (Issue 10), or
- take possession of and transfer corporate books to a new liquidator (Issue 11).

4.3.2 Issue 10: Replacing a liquidator

The Referred Proposal is that:

> ASIC should be able to apply to a court to replace a liquidator if the liquidator dies or is no longer registered.

Background

The members (in a members' voluntary winding up[91]) or creditors (in a creditors' voluntary winding up[92]) may fill any vacancy in the office of liquidator, which may be caused if that person ceases to be a registered liquidator[93] or resigns or dies.

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86 *ASIC Act* s 15.
87 s 1315(1)(a).
88 s 470.
89 s 476.
90 s 533.
91 s 495(3).
92 s 499(5).
93 s 532(1).

The court also has a power to appoint a liquidator to fill a vacancy in either form of voluntary winding up.[94] Only the court may appoint a replacement liquidator in a court winding up.[95] The court rules permit ASIC, as well as other parties, to make an application for the appointment of a liquidator in any of these circumstances.[96]

Policy considerations

The question is whether ASIC should be given a statutory right to apply for a replacement liquidator, rather than this matter being left to the court rules.

On one view, any legislative amendment of this nature should not place an obligation on ASIC to monitor liquidations and apply for replacement liquidators.

Advisory Committee provisional position

> PP10
>
> It is unnecessary to give ASIC a statutory right to apply to a court to replace a liquidator if the liquidator dies or is no longer registered.

Reason

The power of ASIC to apply under the current court rules appears to be sufficient.

4.3.3 Issue 11: Taking possession of and transferring books

The Referred Proposal is that:

> ASIC should be able to take possession of books relating to a company in external administration, and transfer those books to another liquidator, if a liquidator dies or is no longer registered.

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94 s 502.
95 s 473(7).
96 See, for instance, *Federal Court (Corporations) Rules 2000* r 7.2, *Supreme Court (Corporations) Rules 1999* (NSW) r 7.2.

Background

Voluntary administration

When a company is placed into administration, the directors are required to assist the administrator with his or her investigation of the company and its affairs. To this end, as soon as practicable after the administration begins, the company's directors must deliver to the administrator all books[97] in their possession that relate to the company.[98]

Similarly, other persons in possession of books of the company (for instance, the company solicitor or accountant) must give those books to the administrator on being served with a written notice, unless they can establish an entitlement to retain possession of the books.[99]

Liquidation

Current as well as former officers of a company have obligations, similar to those in a voluntary administration, to deliver books to the liquidator.[100]

ASIC powers

ASIC does not have a generic power to require the production, and to take possession, of books. Its powers in this regard can only be used in support of its enforcement and other functions and powers.[101] Even in that context, it does not have a general power to transfer books to another person.

Policy considerations

The concern underlying the Referred Proposal is that the security of these books may be in jeopardy where there is a temporary vacancy in the office of administrator or liquidator.

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[97] The term 'books' is defined broadly in s 9. It includes:
- a register
- any other record of information
- financial reports or financial records, however compiled, recorded or stored, and
- a document (the term 'document' is defined in the *Acts Interpretation Act 1901* s 25).

[98] s 438B(1). This obligation is subject to some rights to retain books.

[99] s 438C.

[100] ss 530A, 530B.

[101] *ASIC Act* Part 3 Div 3.

Advisory Committee provisional position

> PP11
>
> Any interested party should have the right to apply to the court for directions about the temporary holding of books.

Reasons

The key concern is to ensure the security of books of a company in external administration. The right to apply to the court for directions about books should extend to any interested party, including ASIC.

4.4 Request for submissions

The Advisory Committee invites comments on any aspect of the matters raised in this chapter, including the Advisory Committee provisional positions on Issues 7 to 11 and the related issues.

5 Receivers and other controllers

This chapter considers issues specifically related to receivers and other controllers, namely who should be classified as a controller and whether all transactions entered into by receivers and other controllers should be exempt from the voidable transaction provisions.

5.1 Overview

Where a company defaults on a charge that it has given over its property, the chargeholder can appoint a receiver or some other controller to take possession of the company's property subject to the charge, for the purpose of recovering funds owed to the chargeholder.

The notion of 'controller' covers receivers, receivers and managers, and other persons in possession or control of property for the purpose of enforcing a charge.[102]

The terms of reference raise issues concerning:

- who should be classified as a controller (Issue 12)
- whether transactions entered into by receivers and other controllers pursuant to their powers should be exempt from the voidable transaction provisions (Issue 13).

5.2 Classification as controller

5.2.1 Issue 12: Exemption from classification as controller

The Referred Proposal is that:

> The definition of 'controller' should be revised such that enforcing a security over a single asset, or an asset with a value of less than $100,000, does not involve a

[102] s 9 definition of 'controller'.

controllership and the requirements of the Corporations Act dealing with controllers are not applicable.

Background

Receivers and other controllers are subject to various statutory,[103] as well as general law, requirements when acting on behalf of their appointors. For instance, they must:

- lodge with ASIC accounts showing details of their corporate transactions affecting the relevant corporate assets[104]
- take reasonable care to sell property for not less than its market value (if it has a market value) or otherwise the best price reasonably obtainable in the circumstances existing when the property is sold.[105]

There is no provision for exempting controllers from these requirements.

The courts have various supervisory powers over controllers, for instance, to make orders in relation to the exercise of their duties[106] and their obligation to lodge accounts[107] and to remove a controller for misconduct.[108] Controllers can also apply to the court for directions concerning the exercise of their powers.[109]

The issue is whether the statutory obligations applicable to controllers are too onerous for those enforcing the type of securities mentioned in the Referred Proposal (‘relevant security enforcers’). For instance, a bank, or an agent of the bank, simply by enforcing a security over a single piece of real property owned by a corporation, would be a controller.

Is there a need to change the current law?

The argument for no change is that the current provisions ensure that controllers are accountable, act in a proper manner when selling corporate property and are subject to court supervision. For instance:

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103 Part 5.2.
104 s 432.
105 s 420A.
106 s 423.
107 s 434.
108 s 434A.
109 s 424.

- the requirement for controllers to lodge accounts with ASIC ensures that all interested parties can obtain information about how the security has been enforced. Arguably, this outweighs any administrative burden on the security enforcer in lodging this information
- however, if this reporting obligation were lifted, enforcers of real property securities would only be obliged under State and Territory real property legislation to disclose certain information to the mortgagor.[110]

The argument for some change is that the legal obligations imposed on relevant security enforcers may be out of proportion to the 'control' they exercise. This may unnecessarily add to the financier's costs, which are frequently borne by the company, to the detriment of any return to unsecured creditors.[111]

Policy options if change required

Option 1: Total exemption for relevant security enforcers

This option would exempt relevant security enforcers from the statutory obligations applicable to controllers, including in relation to the sale of corporate assets (though mortgagees in possession of real property would remain subject to comparable obligations concerning the sale of corporate assets under common law and other legislative requirements[112]). Also, those persons would not be subject to judicial controls, except in very limited circumstances.[113]

A concern with this option is that the Referred Proposal extends to 'enforcing a security over a single asset'. In some circumstances, the relevant asset could be very substantial. On one view, the proposal should be confined to assets with a value of less than $100,000.

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110 For instance, *Property Law Act 1974* (Qld) s 84, *Real Property Act 1900* (NSW) ss 57, 58 and *Conveyancing Act 1919* (NSW) ss 111, 115A, *Transfer of Land Act 1958* (Vic) ss 76, 77, *Real Property Act 1886* (SA) ss 132, 133, *Transfer of Land Act 1893* (WA) ss 106, 108.

111 Australian Finance Conference Submission on the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007, Issue 1.

112 See, for instance, the analysis of the relevant case law in *Benzlaw & Associates Pty Ltd v Medi-Aid Centre Foundation Ltd* [2007] QSC 233 at [118] ff.

113 For instance, the court power to make a declaration whether a receiver or other person acting to enforce a security is acting validly: s 418A.

Option 2: Partial exemption for relevant security enforcers

Under this option, relevant security enforcers would be exempted from the requirement to lodge accounts,[114] though not from the statutory duty when exercising the power of sale or the supervisory powers of the court.

An argument for this option, particularly for low value assets (less than $100,000), is that the current reporting requirements merely increase the cost of a controllership.

The concern about high value single assets mentioned under Option 1 applies equally to this option.

Advisory Committee provisional position

PP12

There should be no amendment to exempt from the definition of controller a person enforcing a security over a single asset or an asset with a value of less than $100,000.

Reasons

The exemption suggested in the Referred Proposal would not necessarily apply only to cases where the asset in question is a relatively minor part of the company's assets. A single asset could be significant in any administration, while the proposed monetary amount ($100,000) could be significant in a small administration. Also, providing a partial exemption by removing the requirement to lodge accounts would deny interested parties access to this information, while possibly providing minimal real savings, given that the controller would still have to account in some manner to the appointor.

5.3 Voidable transactions

5.3.1 Context

Transactions by receivers or other controllers[115] as agents of the company after their appointment under a charge, but before the

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[114] s 432.
[115] A 'controller' in relation to property of a corporation is defined (s 9) to mean:

winding up begins, are subject to the voidable transaction provisions, which give the court the power to unwind these transactions. However, transactions by controllers in their own right, even when using proceeds from the sale of corporate assets, are not subject to those provisions.[116] Also, all transactions entered into by controllers after the winding up begins are not subject to those provisions.[117]

5.3.2 Issue 13: Exemption from voidable transaction provisions

The Referred Proposal is that:

> Transactions conducted under the authority of a receiver or [other] controller should be exempted from the voidable transaction provisions.

Background

Application to transactions by controllers

The typical transaction at which the Referred Proposal is directed is a payment of commercial necessity made prior to any liquidation by a receiver appointed by a bank to take control of a company's property. The receiver may want to pay old debts of the company without the constraints of the voidable transaction provisions, for instance:

- to ensure the continuing co-operation of creditors who are essential to the completion of a project (for instance, subcontractors)
- to prevent reservation of title creditors from repossessing goods that are essential to the continuation of the business.

- a receiver, or receiver and manager (see ss 90, 416), of that property (defined in ss 9, 416), or
- anyone else who (whether or not as agent for the corporation) is in possession, or has control, of that property for the purpose of enforcing a charge.

116 *Sheahan v Carrier Air Conditioning Pty Ltd* (1997) 189 CLR 407.

117 This is the effect of s 588FE. A receiver has various powers to carry on a corporation's business during a liquidation: s 420C.
Also, transactions by receivers are not subject to the void dispositions provision in s 468 (which applies to dispositions after the commencement of the winding up), given that the company no longer has a beneficial interest in the relevant property: A Keay, *McPherson: The Law of Company Liquidation* (4th edn, LBC Information Services, 1999) at 225. Presumably the same law would apply to transactions by other controllers.

Duties of controllers

Controllers have duties to the parties for whom they act. Unlike administrators and deed administrators, their role is not to act in the general interest of unsecured creditors, but to recover or liquidate property for the benefit of their appointors.

However, controllers are subject to various duties that impose some limitations on their conduct:

- they have statutory and general law duties in exercising a power of sale[118]
- they are subject to the supervision of the court.[119]

In addition, receivers or receivers and managers, being officers of the company, are subject to the statutory duties of officers.[120]

Policy considerations

Two submissions on the Exposure Draft of the Insolvency Bill put forward the Referred Proposal.[121]

One respondent[122] argued that no transactions entered into by receivers or other controllers within their powers should be treated as voidable transactions, given that:

- third parties may be less willing to enter into transactions with receivers or only be willing to transact at a lower price. In consequence, unsecured creditors face a reduced return as, in normal circumstances, they will receive no dividend unless the secured creditor is paid in full
- where there is an administrator, third parties may insist on the receiver obtaining the authority of the administrator to enter into

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118 They have a statutory duty of care in exercising a power of sale to obtain at least market value, where this exists, or otherwise the best price reasonably obtainable in the circumstances: s 420A. They are also subject to some additional general law duties in exercising a power of sale, including that they act in good faith, not sacrifice the mortgagor's interests recklessly, act in accordance with the conditions of appointment and account to the mortgagor for the transaction: *Expo International Pty Ltd v Chant* [1979] 2 NSWLR 820 at 834.

119 s 423.

120 Principally ss 180–184.

121 Australian Bankers' Association, Henry Davis York.

122 Australian Bankers' Association.

certain transactions (given that transactions by the administrator or under the administrator's authority are exempt from the voidable transaction provisions),[123] leading to:

  – delays

  – increased risk of conflict between insolvency practitioners

  – a fundamental policy shift away from the paramountcy of a secured creditor's rights during an administration

- third parties may require indemnities in sale contracts to cover the possibility of the transaction later being set aside. In consequence, receivers may need to delay their retirement, even after the secured creditor has been paid in full, and/or retain substantial excess funds, until the limitation period for voidable transactions has expired, to the detriment of unsecured creditors.

Additional arguments for not subjecting transactions by receivers or other controllers to the voidable transaction provisions are:

- a receiver may have an interest in preserving the business for the longer term benefit of the secured creditor and therefore should not be hampered by the voidable transaction provisions in dealing on behalf of the company

- abuse of the exemption (for instance, where the receiver is appointed pursuant to a security held by a director-controlled related entity and makes payments to the directors) may constitute a breach of the fiduciary duty owed by the receiver or other controller to the company

- controllers already have a statutory duty in exercising a power of sale to obtain at least market value, where this exists, or otherwise the best price reasonably obtainable in the circumstances.[124]

Arguments for subjecting transactions by receivers or other controllers to the voidable transaction provisions are:

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[123] The same point was raised by Henry Davis York Submission para 7.4.

[124] s 420A.

- there is the potential for abuse, as controllers, unlike administrators and deed administrators, are not required to act in the interests of unsecured creditors

- exempting these transactions may enable some unsecured creditors to negotiate a more favourable arrangement for payment of outstanding debts, contrary to the pari passu principle[125]

- the chances of success in an action for breach of a fiduciary duty or a duty in exercising the power of sale are much lower than in an action to unwind transactions under the voidable transaction provisions.

Policy options

These include:

- *Option 1:* adopt the Referred Proposal to exempt all transactions by receivers or other controllers from the voidable transaction provisions

- *Option 2:* adopt the Referred Proposal, except for uncommercial transactions, which would remain subject to the voidable transaction provisions. This option would prevent a receiver from effecting a form of informal foreclosure by selling the asset at a significant undervalue to the receiver's appointor

- *Option 3:* only exempt from the voidable transaction provisions any payment by controllers to the supplier of an 'essential service'.[126]

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[125] Compare *Sheahan v Carrier Air Conditioning Pty Ltd* (1997) 189 CLR 407 per Kirby J (dissenting) at 463–464 who recognised 'the important social and commercial purposes of the sections, being designed to protect creditors against any attempt to favour one creditor or group of creditors over others during the time immediately before winding up'. He also observed:

> there would be serious consequences for unsecured creditors in a less powerful bargaining position although equally deserving of payment once the debtor company became insolvent. … The payments to [some] creditors from the funds of the company necessarily reduce the amount of funds available to pay other creditors. If a principle were established which would permit such payments to stand outside the power of recoupment by a liquidator [under the voidable transaction provisions], the pari passu principle, which lies at the very core of the administration of insolvency law, would be subverted.

[126] As defined in s 600F.

Advisory Committee provisional position

> **PP13**
>
> Transactions conducted under the authority of a receiver or other controller should be exempted from the voidable transaction provisions.

Reasons

It is appropriate to exempt transactions by receivers and other controllers from the voidable transaction provisions (Option 1), even if this reduces the possible return to general unsecured creditors, as:

- it is desirable to provide commercial certainty to counterparties whose transactions can affect the ongoing viability of the company
- the voidable transaction provisions are more suited to regulating the actions of directors or other officers of an ongoing company
- the possibility that transactions may be voided could reduce the market value of a company's assets
- receivers and other controllers are subject to statutory and general law duties in exercising the power of sale
- receivers and other controllers are subject to the supervision of the court.

Exempting these transactions from the voidable transaction provisions would also remove any difference in result depending on whether the transactions are entered into by a receiver or other controller as agent of the company (subject to the voidable transaction provisions) or in their own right (not so subject).

There are also additional protections where the controller is a receiver:

- receivers have duties as officers of a company

- receivers must be registered liquidators[127] and therefore are subject to the jurisdiction of the Companies Auditors and Liquidators Disciplinary Board.

5.4 Request for submissions

The Advisory Committee invites comments on any aspect of the matters raised in this chapter, including the Advisory Committee provisional positions on Issues 12 and 13.

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127 s 418(1)(d).

6 Matters affecting several forms of external administration

This chapter considers issues applicable to more than one form of external administration, namely the provision of information concerning an external administration to the general public and electronic communication with creditors.

6.1 Provision of information to the general public

6.1.1 Overview

The terms of reference raise two issues concerning how information about companies in external administration is to be provided to the general public:

- whether the requirements to publish insolvency or other external administration notices could be streamlined through use of the Internet (Issue 14)
- whether the right to ask the court for an exemption from the requirement for a company in external administration to publish its former name should be extended beyond a deed administrator to all external administrators (Issue 15).

6.1.2 Issue 14: Publication of external administration notices

The Referred Proposal is that:

> The requirement to publish insolvency notices in a newspaper should be limited, such that it requires only a summary statement with additional details to be published on a website to be maintained by ASIC or a professional body. An alternative proposal would move all notices to a website to be maintained by ASIC or a professional body.

Background

The external administration process involves a series of obligations, on external administrators or others, depending on the

circumstances, to disclose publicly specified information related to the affairs of the company. In each case, the information must be disclosed in newspapers (print).

Public notices of insolvency proceedings in court include:

- notice of application for an order that a company be wound up[128]
- notice of an order substituting the plaintiff in an application for a winding up order[129]
- notice of the making of a winding up order and appointment of a liquidator[130]
- notice of appointment of a provisional liquidator[131]
- notice of application by a liquidator for special leave to distribute a surplus.[132]

Other public notices relating to external administration include:

- notice that a company has appointed an administrator[133]
- notice of creditor meetings in a voluntary administration[134]
- notice to submit particulars of a debt or claim[135]
- notice to submit a formal proof of debts or claims.[136]

These public disclosure obligations are in addition to obligations on external administrators to communicate directly with known creditors (discussed in Issue 16).

128 Harmonised Corporations Rules: rule 5.6(2)(b).
129 rule 5.10(2)(b)(i).
130 rule 5.11(4)(b).
131 rule 6.2(4)(b).
132 rule 7.9(3)(b).
133 s 450A.
134 s 439A(3)(b), Corp Reg 5.6.14A.
135 Corp Reg 5.6.39.
136 Corp Reg 5.6.48.

Policy considerations

Overview

The Referred Proposal raises the issue of whether, or to what extent, the Internet should replace print media as the means of publishing the range of public notices arising from external administrations. The Referred Proposal refers to public insolvency notices, but the discussion in this paper has been extended to all public external administration notices. This review does not consider the scope or content of these notices.

Options to amend the current requirements for public external administration notices include:

- *Option 1:* retain the print disclosure requirements and add an Internet disclosure requirement
- *Option 2:* abbreviate the print disclosure requirements and add an Internet disclosure requirement (the first option in the Referred Proposal)
- *Option 3:* discontinue the print disclosure requirements, and require only Internet disclosure (the second option in the Referred Proposal).[137]

Each of the options contemplates some form of Internet disclosure of public notices associated with external administrations. In each case, this could be on a designated website, administered by ASIC or some other public regulatory body, for the lodgement of these notices. External administrators and other persons could also choose to place these public notices on other websites (for instance, the website of the company under external administration). However, requiring all public notices associated with external administrations to be lodged on a designated external administration website would ensure that all these notices are publicly accessible at one location.

Possible precedents for this type of website are the Company Alert System administered by ASIC or the proposed single national online register of personal property security interests.[138]

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[137] Compare The Insolvency Service (UK), *Consultation Paper* (September 2007), Proposal 3, which would enable ‘the liquidator to publicise the liquidation in whatever way he considers it would come to the attention of any additional creditors’, for instance, publication on the company’s website or the website of a relevant association.

Consideration of options

The first option, to retain the current print disclosure requirements and add an Internet disclosure requirement, would maximise the possibility of interested persons becoming aware of information currently found in public notices. However, it would not result in any reduction in the requirements for print notices, the costs of which could reduce the funds available to general creditors in an external administration.

The second option, to abbreviate the print disclosure requirements, with the added Internet disclosure requirement, may result in some cost savings, depending on what level of abbreviation is permitted.

The third option would result in the greatest cost reduction by relying on the Internet as the forum for public disclosure.

An argument for placing greater emphasis on the Internet as the preferred public disclosure forum is that print notices, even if they appear in a number of separate newspapers, are generally only available on the day of publication and are not readily searchable through electronic technology. By contrast, online information can be retained indefinitely and be fully searchable.

One possibility is to adopt a phased process whereby, over time, the Internet becomes the sole method for publishing all public notices related to external administrations, for instance:

- step 1: combined print and Internet publication of these public notices, possibly moving over time from Option 1 to Option 2
- step 2: a review at some stage after the adoption of step 1, to determine if and when it would be appropriate to adopt Option 3
- step 3: adopt Option 3 by requiring Internet publication only, on a designated website, of these public notices.

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[138] Attorney-General's Department Review of the law on Personal Property Securities, *Discussion Paper: Registration and Search Issues* (November 2006) at para 356.

Advisory Committee provisional position

PP14

There should be a staged move from print media to Internet disclosure of all public notices on a designated website to be operated by ASIC.

Reasons

Electronic publication is potentially a more effective way to disclose information in an easily accessible and retrievable form. It also affords considerable savings in cost and time. A move to Internet disclosure may enhance economic efficiency, provided that there is an appropriate transitional period to allow persons affected to adjust.

It will be open to external administrators to choose to publish notifications in the print media or on other websites (for instance, that of the company under external administration). Furthermore, the public will continue to be made aware of corporate developments through media articles.

Information to be disclosed on the designated website would include details about the creditors of a company in voluntary administration (if PP1 were adopted).

6.1.3 Issue 15: Exemption from publication

The Referred Proposal is that:

> The rule allowing a deed administrator to apply to the court for an exemption from the rule requiring a company to publish its former name on public documents should be extended to all other types of external administration.

Background

In consequence of amendments operative from July 2008, a company in external administration that changes its name[139] during, or six months prior to, the external administration will be required to disclose its former name as well as its current name on public

[139] From July 2008, following enactment of the *Corporations Amendment (Insolvency) Act 2007*, liquidators, administrators, deed administrators and managing controllers will be able to lodge an application with ASIC to change a company's name without the need for a special resolution of members, provided it is in the interests of the creditors as a whole: s 157A.

documents, for the period of the administration or any subsequent liquidation.[140]

It was intended that a deed administrator would have the right to apply to the court for an exemption from this disclosure requirement.[141] The court could grant the exemption:

> if it is satisfied that the granting of leave will not result in any significant risk to the interests of the company's creditors (including contingent or prospective creditors) as a whole.[142]

The question raised by the Referred Proposal is whether this right to apply to the court should also be given to an administrator, a receiver or other controller, or a liquidator.

The Referred Proposal does not affect the separate requirement to disclose in public documents that a company is in external administration.[143]

Policy considerations

Arguments that administrators, receivers and other controllers and liquidators, not just deed administrators, should have the right to apply to the court for an exemption from the requirement to disclose a former name are:

- this disclosure requirement may adversely affect the ability of those persons to sell the business of a company that is in external administration[144]

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[140] s 161A. This provision implements a recommendation of the Advisory Committee: *Corporate voluntary administration* (June 1998) rec 60. As with the amendment introducing s 157A, s 161A will commence operation from July 2008. By contrast, the majority of the amendments under the *Corporations Amendment (Insolvency) Act 2007* were operative from 31 December 2007.

[141] Due to an apparent error, the power has been given in relation to a company under administration, rather than one subject to a deed of company arrangement: s 161A(3) refers to s 161A(1)(b)(iii) (company under administration) rather than s 161A(1)(b)(iv) (company that has executed a deed of company arrangement).
However, s 161A(6) says that the court 'may only grant leave … on the application of the administrator of the deed of company arrangement' and para 4.233 of the Corporations Amendment (Insolvency) Bill 2007 Explanatory Memorandum makes it clear that the deed administrator was the intended recipient of the power.
Given the clear intention of Parliament to give the right to a deed administrator, the court may be prepared to exercise its discretionary power (s 447A) to modify the law and grant a deed administrator leave to omit a company's former name.

[142] s 450E(5).

[143] See, for instance, s 450E.

- a court exemption from disclosure may maximise the chances of a better return for past creditors of the company, for instance, by facilitating the attraction of new equity or loan capital
- if a company has new owners, it may not be necessary to put future creditors dealing with the company on notice that the company is one that, under its previous owners and with a different name, was in external administration: it is appropriate to allow the court to decide this matter
- in the case of administrators, it would give the court a specific power to do what it can do under its general modification power.[145]

A contrary view is that existing and future creditors are entitled to be informed of any former name under which the company has traded in the recent past. This information may better enable them to assess the company's past performance.

Another view is that the need to apply for an exemption from disclosure may be greater for some types of external administrator than for others. For instance:

- there may be merit in extending this right to a receiver, who may have a legitimate need to sell the company's business and goodwill, but find that the value of the company's shares is unduly reduced by a negative commercial reputation associated with the former company name that is not relevant to the future performance of the company
- by contrast, there may not be the same need to enable liquidators to apply to the court, given that there is not the same rationale for attracting new investment in the company
- also, it may be unlikely that an administrator would need this power in the period before a company that is in voluntary administration adopts a deed of company arrangement.

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[144] Insolvency Practitioners Association Submission on the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007, para 14.1.1.

[145] s 447A. See *Re Brashs Pty Ltd* (1994) 15 ACSR 477 at 483, 13 ACLC 110 at 115-116 per Hayne J.

Advisory Committee provisional position

PP15

Administrators, receivers and other controllers and liquidators, as well as deed administrators, should have the right to apply to the court for an exemption from the rule requiring a company to publish its former name on public documents. In exercising its discretion whether to grant an application, the court could take into account the possible prejudice to relevant parties, including past creditors and persons who may have to deal with the company in the future.

Reason

All external administrators should have the right to apply to the court for an exemption from the rule requiring a company to publish its former name on public documents, given that the court can consider the particular circumstances of each case in deciding whether an exemption is justified.

6.2 Communication with creditors

6.2.1 Context

Administrators must give written notice of meetings to identifiable creditors of a company in voluntary administration.[146] Similar obligations of personal notification apply in liquidations.[147] In some circumstances, deed administrators may also need to communicate with creditors.[148]

These obligations of personal notification are additional to the obligation to provide information through public notices (see Issue 14).

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[146] s 439A(3)(a). However, administrators do not have a duty to seek out and notify non-obvious creditors: *Selim v McGrath* (2003) 47 ACSR 537 at [125]-[135].

[147] For instance, ss 496(2), 497(1), (2).

[148] For instance, s 445F. Also, PP4 (Section 3.2.2) proposes that the deed administrator be required in some circumstances to notify creditors of a breach of a DOCA.

6.2.2 Issue 16: Electronic communication with creditors

The Referred Proposal is that:

> The new mechanism for electronic communication with creditors should be extended, to allow for electronic means to be used except if the creditor requests a hard copy of documents. One suggested approach would provide for a single page to be sent to creditors directing them to documents available on a website and providing a telephone number to call if a hard copy is required. An alternative proposal would provide for a creditor being 'deemed' to have consented to electronic communication where a company has communicated with a creditor by that means at any time prior to the commencement of the external administration.

Background

Under amendments operative from 31 December 2007 (the 'new mechanism for electronic communication with creditors' mentioned in the Referred Proposal), creditors can 'opt in' to receive electronic communications from administrators, deed administrators or liquidators (external administrators) in that:

- creditors can nominate:
  - a fax number, electronic address or other electronic means for the receipt of notices and documents, or alternatively
  - an electronic means for being notified of the availability of notices or documents and an electronic means by which they can obtain access to those notices or documents
- the external administrator is entitled to use the nominated means for all notices or other documents during the course of the external administration
- notices and documents conveyed by the nominated means are taken to be given or sent on the next business day.[149]

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[149] s 600G, Corp Reg 5.6.11A.

Issues with the creditor 'opt in' approach

Giving external administrators the ability to communicate electronically with creditors may increase efficiency and save time and administrative costs, with a consequential likely increase in funds available for distribution to creditors.[150]

However, the Insolvency Practitioners Association has argued that the 'opt in' system for electronic communication with creditors may not be fully effective, in that:

- there is no incentive for creditors to elect to receive electronic communications
- unless all creditors elect to receive information electronically, the external administrator will have the added burden of sending some information electronically and some in paper form.

Also, electronic addresses such as email are usually person-specific and an entity may not receive an email if the relevant person leaves the organization.

Advisory Committee provisional position

PP16

External administrators should be permitted to advise in their first notification to each creditor that all further notices to creditors and other documents relevant to the external administration will be published on one or more websites (which must include the designated ASIC website for public documents, as discussed in Issue 14).

That first notification should also state that any creditor may choose to register:

- to receive an electronic notification that new material has appeared on the website(s), or
- to receive by mail, free of charge, a printed copy of these further notices and other documents.

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150 The Ansett administrators estimated that it would cost approximately $28 million to send the notice of the major meeting and accompanying documentation to the approximately four million creditors of Ansett.

> Creditors who so register will continue to receive information in the specified manner unless they subsequently notify the company that they no longer wish to do so.

Reasons

This approach is consistent with that recommended by the Advisory Committee in its report *Rehabilitating large and complex enterprises in financial difficulties* (2004). The Committee gave the following reasons for that approach:

> It is in the interests of creditors for administrators to use the most inexpensive and efficient means to provide them with information. In particular, the onus should be on creditors, once initially informed by written notice, to request further documentation (for instance, by use of the toll-free telephone number) or download it themselves from the administrator's website, rather than receiving it automatically. Making information available in this way should ensure that creditors can obtain the information at little or no cost to themselves. Overseas contactable creditors would not be unduly disadvantaged, given that they would receive the initial written notice and thereafter could access at least the website.[151]

The provision for creditors to register to receive electronic notification of new material, rather than to receive electronic versions of the material itself, would avoid possible technical difficulties, particularly in sending or receiving large documents by electronic mail. This aspect of the Advisory Committee's provisional position differs from the procedure introduced on 31 December 2007, which contemplates individual creditors who so elect receiving all documents electronically.

6.3 Request for submissions

The Advisory Committee invites comments on any aspect of the matters raised in this chapter, including the Advisory Committee provisional positions on Issues 14 to 16.

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151 para 2.5.