Australian Government

Corporations and Markets Advisory Committee

ISSUES IN EXTERNAL ADMINISTRATION

Report

November 2008

Corporations and Markets **Advisory Committee**

Issues in external administration

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ISBN 978-0-9805232-1-8 (print version)
ISBN 978-0-9805232-2-5 (on-line version)

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28 November 2008

Senator the Hon Nick Sherry
Minister for Superannuation and Corporate Law
Parliament House
CANBERRA ACT 2600

Dear Minister

I am pleased to present a report by the Advisory Committee on *Issues in external administration*.

Yours sincerely

Richard St. John
Convenor

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1 Introduction

This chapter explains the background to the review, sets out the terms of reference, outlines the structure of the report and provides information about the Committee.

1.1 Background

As part of the process that led to the enactment of 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, which became effective from 31 December 2007.[1]

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

1.2 Referral of issues

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* (1998), *Corporate Groups* (2000) and *Rehabilitating large and complex enterprises in financial difficulties* (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 has released a discussion paper *Members' schemes of arrangement* (June 2008), which covers this topic as well as broader questions relating to members' schemes.

1.3 Review process

In February 2008, the Advisory Committee published a discussion paper *Issues in external administration*, which invited submissions on the matters that had been referred to the Committee and the Committee's provisional position on each of those matters.

The Committee received submissions from:

- Professor Michael A Adams and Marina Nehme (Adams and Nehme)

- Australian Securities and Investments Commission (ASIC)

- A Hargovan

- Australian Finance Conference and Australian Equipment Lessons Association (AFC)
- Australian Institute of Credit Management (AICM)
- Geoffrey McDonald
- Insolvency Practitioners Association (IPA)
- Commercial Law Association—Legislative Review Taskforce (CLA)
- Law Council of Australia—Insolvency and Reconstruction Committee (LCA)
- Australian Credit Forum (ACF)
- Robert M H Cole & Co (Robert Cole)
- The Law Society of NSW.

These submissions are available on the Advisory Committee's website. In preparing this report, the Committee closely considered the matters raised by the respondents. The Committee was greatly assisted by the submissions and thanks all respondents for their efforts.

1.4 Structure of report

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

The issues on which the Advisory Committee was asked to comment 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)
- information issues in external administration (Chapter 6, Issues 14–16).

The report sets out the background to each issue, relevant policy considerations, the Advisory Committee's provisional position, a summary of submissions on that position and the Advisory Committee's recommendation.

1.5 Advisory Committee

The Advisory Committee is constituted under 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
- Jeremy Cooper—Deputy Chairman of the Australian Securities and Investments Commission
- Ian Eddie—Professor of Accounting, School of Commerce and Management, Southern Cross University, Tweed Heads
- Alice McCleary—Company Director, Adelaide
- Marian Micalizzi—Chartered Accountant, Brisbane
- Geoffrey Nicoll—Co-Director, National Centre for Corporate Law and Policy Research, University of Canberra, Canberra
- Ian Ramsay—Professor of Law, University of Melbourne
- Robert Seidler—Partner, Blake Dawson, 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, 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
- Thaumani Parrino—Office Manager.

2 Forms of external administration

By way of background, this chapter summarises 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 Company-initiated external administration

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 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. They may agree to the company returning to active trading, restructuring its affairs under a deed of company arrangement (DOCA) or 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.

2.2.3 Voluntary winding up

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

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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).

This 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 others

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 Definition of 'controller' in s 9.

12 ss 459A, 459P.

13 ss 461–464.

3 Voluntary administration

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

3.1 Duties of 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 eight business days after the administration begins, with creditors to receive notice at least five 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 raised questions about whether the administrator should be required to:

- provide access to a list of a company's known creditors (Issue 1)
- provide details of the location of equipment in the possession of the company, but owned by others (Issue 2)
- chair the major meeting in person (Issue 3).

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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.

3.1.2 Issue 1: Access to creditor list

The Referred Proposal was 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 way of comparison, 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 addresses of those creditors, and
- the estimated amounts of their claims[18]

as shown in the records of the company. However, if the debt owed to a creditor is less than $1,000, the liquidator only needs to specify to that creditor where a copy of the list may be obtained, unless the court otherwise orders.[19]

Arguments for and against change

Arguments for making some change to the current position in relation to a voluntary administration are:

- other creditors may wish to know who else is owed money by the company

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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).

- 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]

Arguments against any change are:

- some creditors may be concerned about the disclosure of commercially sensitive financial information
- a list may encourage proxy hunting by creditors
- a requirement to provide the list may increase administrative costs
- a list could make it easier for other insolvency practitioners to lobby creditors to replace the administrator.

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

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

Policy options on information to be disclosed

The policy options in relation to a voluntary administration 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 of the identity of fellow creditors without undue administrative burden or cost (given that the administrator is already required to ascertain the identity of the company's creditors

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

prior to the first meeting to give them written notice of the meeting[21]).

Option 2: Names, contact details and amounts

Arguments for disclosing the estimated value of debts as well as the identity of 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
- provide known creditors with relevant information without placing the onus on them to obtain it.

Also, to the extent that commercial sensitivity about disclosure may be an issue, details of creditors' names, addresses and amounts owed are already required to be disclosed to other creditors in a voluntary insolvent winding up.[22]

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.[23]

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).

21 In accordance with s 436E(3).
22 ss 496(2), 497(2).
23 The Australian Bankers' Association, on whose submission the Referred Proposal was based, did not favour disclosure of the amount of debts: para 9.8.

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

- it would avoid undue administrative cost
- it may alert creditors who are unknown to the administrator
- 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 was:

> 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 Committee also sought submissions on whether disclosure of estimated amounts, if required, might be simplified by requiring disclosure within designated bands, rather than disclosure of the specific amount due, to reduce commercial sensitivity.

Submissions

The majority of respondents supported the approach in PP1 of publishing a list of the creditors of a company in voluntary administration on a designated website.

The ACF suggested that PP1 was unnecessary, as the name, address and amount owed should already be on the public register in accordance with industry guidelines.

The LCA opposed PP1, suggesting a more limited approach whereby the list of creditors, and relevant details, would be available only to a limited group of persons on written request.

Some respondents who supported PP1 made additional comments as follows.

Information to be disclosed

Suggestions for modifying PP1 included:

- the administrator's obligation should only require disclosure to the best of the administrator's knowledge, given the limited time for collecting the information,[24] or
- a creditor should have the ability to limit the amount of private information published to other creditors,[25] or
- creditors should have the option of giving a specific or standing written instruction to remove their contact details from the list.[26]

Timing of disclosure

The IPA observed that the ability of administrators to comply with the requirement to publish information on the website 'no later than the time of distribution to creditors of the notice of the first meeting' would depend on the state of the company's records and the administrator's ability to convert information into a format suitable for publication on the Internet.

Recipients of information

Various respondents raised a concern whether creditors, for commercial privacy reasons, may prefer their details not to be made generally available. The NSW Law Society Business Law Committee suggested that the website should be password protected.

Banding of debts

There was little support for the banding of debts. While one submission[27] suggested that banding may make the administrator's job easier, most respondents opposed it, given the cost and the administrative burden that it might impose in the limited time for collecting the information about creditors.[28]

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24 IPA, AICM.
25 CLA.
26 NSW Law Society Business Law Committee.
27 Adams and Nehme.
28 IPA, LCA, NSW Law Society Business Law Committee, AICM.

Advisory Committee recommendation

Recommendation 1

In a voluntary administration, the administrator should publish on a designated website, no later than the time of distribution to creditors of the notice of the first meeting, information known to the administrator concerning the name and contact details of each creditor.

The administrator should also publish on that website the estimated amount due in relation to each creditor of the company, other than in relation to any creditor who indicates to the administrator that the amount due to that person should not be made public.

This recommendation modifies PP1 by permitting an opt-out whereby the amount due to a creditor would not be disclosed on the website if the creditor indicated to the administrator that the information should not be made public.

Reasons for recommendation

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 relevant information about their fellow creditors to assist them in that process.

Publication of information on the Internet would be simple to administer and would avoid the cost of mailing information to creditors.

An opt-out provision would allow creditors the opportunity to protect their commercial privacy regarding the amount owed to them by the company. This would remove any need for the designated website to be password-protected.

The Committee is mindful that a liquidator in a voluntary winding up must provide various details to all creditors, including the estimated amounts of each creditor's claim, with no right for individual creditors to opt out. However, the liquidation requirement involves disclosure to creditors only, whereas Recommendation 1 involves disclosure on a publicly accessible website.

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

3.1.3 Issue 2: Notice to property owners

The Referred Proposal was 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

An administrator needs to consider whether the company will retain any equipment or other property in the company's possession that is owned by a third party.[29]

An administrator who decides not to retain such property may notify the owner of that decision within five business days after the commencement of the administration.[30] 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 five business day period,[31] subject to indemnity rights against the company's property.[32]

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

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29 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 reservation of title (Romalpa) clause, which provides that title to goods does not pass from the vendor to the purchaser until they have been paid for.

30 s 443B(3).

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

32 s 443D.

Elements of the Referred Proposal

The proponent of this proposal[33] suggested 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.

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 companies that have leased property have a strong incentive to identify and locate all leased assets, given that they automatically become liable for payments on those assets after a period of time.

Arguments against the proposal are that it is open to the owner of equipment to communicate directly with the administrator to arrange for its recovery or to include in the original lease contract a term requiring disclosure of the location of the equipment.

Advisory Committee provisional position

PP2 was:

> 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

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

> 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.

Submissions

Respondents supported PP2, subject to concern about imposing additional duties on administrators. The LCA suggested that an administrator should only be responsible for indicating the location of property where he or she had personal knowledge of where it was located. Administrators should not have a positive duty to locate property.

Advisory Committee recommendation

Recommendation 2

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.

It should be made clear that administrators have no duty to search for property. While administrators could be expected to facilitate efforts to locate property, they should not be under a duty to search for it.

Reasons for recommendation

An owner of property should in principle be informed about the location of that property. An obligation only to provide information that 'is reasonably available to the administrator' should minimise the burden on administrators.

3.1.4 Issue 3: Chairing the major meeting

The Referred Proposal was 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

Insolvency practitioners may generally send a nominee in their place to chair meetings of creditors.[34] However, an administrator is required to chair the major meeting of creditors in a voluntary administration.[35] This presumably 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 major meeting of creditors, 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 regarding the major meeting of creditors is that a requirement for court approval to 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 an administrator having 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
- 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.

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34 Corp Reg 5.6.17(1).

35 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)).

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[36]
- 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'[37] about the administration
- providing for the adjournment of the meeting 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 was:

> 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
> - 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.

36 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 359–364.

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

> 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.

Submissions

There was general support for permitting an administrator to appoint a suitably qualified nominee when the administrator cannot attend the major creditors' meeting through illness. Some respondents also supported 'some other good reason' as justification for non-attendance and the appointment of a nominee. A number of respondents considered that the current requirement to obtain a court order for such a nomination was costly and slowed the administration process.

A number of respondents supported an administrator having the option to attend a meeting through a videoconference or loudspeaker telephone. This may be useful, for instance, where an administrator needs to travel long distances or attend meetings that may largely be a formality.

The LCA, while supporting PP3, recommended that any notice of the non-attendance of the administrator should be given to ASIC, as the possibility of ASIC review would militate against inappropriate utilisation of this exception.

The CLA considered that where the nominee was an employee, partner or principal of the administrator's firm there should not be any requirement for the passing of a resolution by creditors, but the nominee should advise the meeting of the reason for the administrator's non-attendance.

Robert Cole said that the nominee should be any suitably qualified staff member conversant with the administration, not just a registered liquidator. The requirement for a registered liquidator was impractical and unworkable for a small firm, particularly where the unforeseen circumstances arise close to the meeting, as sole practitioners do not necessarily have a registered liquidator on their support staff.

Advisory Committee recommendation

Recommendation 3

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, where an administrator cannot attend that meeting because of illness or some other good reason, the administrator should have a discretion to nominate a registered liquidator, or a staff member of the administrator's firm, to chair that meeting, with the approval of the creditors.

Before voting on whether the nominee should chair the meeting, creditors should be provided with:

- a statement by the administrator of the reason for his or her inability to attend
- relevant information concerning the nominee's experience in external administrations generally and any professional involvement that he or she has had in the particular administration, and
- a statement by the administrator certifying 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.

This recommendation modifies PP3 by allowing for an administrator to nominate a staff member who is not a registered liquidator to chair the major meeting.

Reasons for recommendation

The Advisory Committee acknowledges the importance of the administrator participating in the major meeting of creditors, but recognises that, in some circumstances, it may be impractical for that to happen. Administrators should have some flexibility to send a nominee to the major meeting, short of a court application, without being able to do so merely for reasons of convenience.

The interests of creditors would be protected by the requirements that they be provided with relevant information and that, in all instances, the nominee would require the approval of the creditors.

The Advisory Committee accepts the submission that it may not always be practicable to have a registered liquidator as the nominee. Small firms and firms in less populous jurisdictions may have only one registered liquidator and may therefore have to incur the expense of bringing in a registered liquidator from elsewhere. A staff member may have a greater knowledge of relevant facts than an external registered liquidator.

The recommendation does not adopt the suggestion that the administrator should be required to inform ASIC within two days after the meeting that he or she had not been able to chair the meeting. There is already a requirement to lodge the minutes of the major meeting, which will show who chaired the meeting.[38]

There is no need for legislative change to enable administrators to attend a meeting by videoconference or loudspeaker phone. In practice, administrators can hold a valid meeting by videoconference or loudspeaker phone, provided that they convene the meeting at the venue where they are located.

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).

A DOCA normally takes the form of 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

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38 Corp Reg 5.6.27.

favour of it.[39] 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.[40]

Creditors bound by a DOCA may not take action against the company or its property without the leave of the court.[41] Also, they cannot make or proceed with an application for a winding up order.[42]

The creditors of a company subject to a DOCA may terminate the deed by resolution if:

- there has been a breach of the deed, and
- the breach has not been rectified before the resolution is passed.[43]

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

The Referred Proposal was that:

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

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

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

41 s 444E(3).

42 s 444E(2).

43 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* (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 (ss 445C(a), 445D), where there exist circumstances in which the deed specifies that it is to terminate (s 445C(c)) or where the administrator certifies that the deed has achieved its purpose (ss 445C(d), 445FA).

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

The discussion paper examined two policy options:

- require deed administrators to inform creditors of all breaches of the DOCA, given their statutory right to terminate it

- require deed administrators 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 was:

> 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.

Submissions

Most respondents generally agreed with PP4.

However, the IPA and the CLA were concerned with giving directors who have resumed control of a company the sole responsibility for reporting any breaches of a deed of company arrangement. They considered that creditors would be better protected by the deed administrator having that responsibility in all instances. The directors should be required to notify the deed administrator of the breach. The deed administrator would then have the obligation to notify the creditors.

The ACF, while favouring giving additional information to creditors, was concerned that any legislative requirement to notify creditors not impose onerous administrative tasks on the deed administrator.

The LCA and the NSW Law Society Business Law Committee suggested notification of material contraventions to creditors as soon as practicable but within 21 days of the breach. At the time of notification, the deed administrator should also be required either to convene a meeting of creditors to vote on the variation or termination of the DOCA, or to set out the reasons for not convening a meeting, together with the proposed course of action.

Advisory Committee recommendation

Recommendation 4

The deed administrator should be required to notify creditors, as soon as it is practicable to do so, of any information known to the deed administrator regarding a breach, a combination of breaches or likely future breaches, that could reasonably be expected to have a material effect on the purpose or outcome of the deed.

If the company subject to the deed is under the control of the directors, the directors must inform the deed administrator of any breach or likely future breach known to them as soon as it is practicable to do so.

This recommendation modifies PP4 by placing the responsibility for notifying creditors on the deed administrator in all instances and by adding a notification requirement for ‘likely future breaches’.

Reasons for recommendation

A requirement to notify creditors of every 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. Recommendation 4 would provide flexibility, so that creditors would only receive information about breaches that are material and ongoing.

Placing the obligation to notify creditors on the deed administrator in all instances ensures that his or her professional skills and judgment are brought to bear on whether a breach would have a material effect on the purpose or outcome of the deed.

The extension to 'likely future breaches' is designed to cover an event that does not immediately constitute a breach of the deed, but may at some future point do so. It therefore ensures that creditors would be notified of emerging problems with a deed rather than being informed only after the breach has occurred. This 'early warning' requirement would also enable creditors to protect themselves from these likely outcomes by ceasing to extend credit or otherwise adjusting the terms on which they provide credit.

3.3 Winding up following an administration

3.3.1 Context

A company under administration goes into winding up if:

- the creditors resolve at the major meeting that the company be wound up,[44] 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 or such further period as the court allows.[45]

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

- the company's creditors resolve to terminate the DOCA and wind up the company[46]
- the court makes an order terminating the DOCA[47]
- the DOCA specifies circumstances in which it is to terminate and the company be wound up and those circumstances exist.[48]

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.[49]

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44 ss 439C(c), 446A(1)(a), (2).
45 ss 444B(2), 446A(1)(b), (2).
46 ss 445E, 445F, 446A(1)(c), (2).
47 s 445D, Corp Reg 5.3A.07(1)(a)).
48 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 was 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 arose from a concern that certain creditors (referred to in this report 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 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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[49] 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* (1998) rec 54 and the Parliamentary Joint Committee on Corporations and Financial Services report, *Corporate Insolvency Laws: a Stocktake* (2004) rec 2.

vote of related creditors set aside on various grounds relating to the overall interests of creditors.[50]

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 (the Referred Proposal)
- *Option 3:* give the former administrator a right of appeal.

Option 1: No change

While there would be no restrictions on voting by creditors, a 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.[51]

Option 2: Prohibition on voting

This approach 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[52] identified competing policy considerations:

- 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 real 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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50 s 600A.
51 ibid.
52 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 a 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, who may also have conflicts of interest, will 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
- a 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:

- 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[53] that refer to the possible commencement of litigation 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 an application to overturn the resolution for removal, in the absence of a court order to the contrary.

Advisory Committee provisional position

PP5 was:

> 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.

The Committee also sought submissions on whether anyone, in addition to a creditor, should have a right to challenge a resolution appointing a new person as liquidator and, if so, what type of remedy should be available.

Submissions

Most respondents supported PP5, on the basis that a rule preventing directors and other related party creditors from voting would operate in an unreasonably harsh manner in most situations and there were already adequate protections.

The IPA, whose submission had led to the Referred Proposal, opposed PP5, on the basis that directors should be bound by their choice of administrator and only independent creditors should decide on the appointment of a different person as liquidator. The same respondent considered that administrators should be able, at their own cost, to challenge a resolution for their removal and request reinstatement.

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53 s 439A(4)(a).

Additional suggestions by respondents who supported PP5 were:

- the chair of the creditors' meeting should declare whether the results of a poll would have been different if the related party creditors had not been allowed to vote and inform those present of their rights to challenge the vote[54]
- where a creditor is voting in respect of an assigned debt, the value for voting purposes should be equal to the value of the consideration the creditor gave for the assignment of the debt.[55]

Advisory Committee recommendation

Recommendation 5

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 for recommendation

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.

The Committee has no problem with the notion that replaced administrators could institute a legal challenge, at their own cost, to the resolution for their removal. It notes that administrators may already have this capacity.[56]

The Committee does not see any practical benefit in the suggestion that the chair of the creditors' meeting should declare

54 LCA, NSW Law Society Business Law Committee.
55 LCA.
56 s 600A.

whether the results of a poll would have been different if the related party creditors had not been allowed to vote.

The Committee does not support the proposal that, where a creditor is voting in respect of an assigned debt, the value for voting purposes should be equal to the value of the consideration the creditor gave for that debt. A change of this nature would have significant adverse implications for the corporate secondary debt market. The commercial value of debt in that market derives from its being bought at a discount to its face value while retaining the full face value for voting purposes.

3.3.3 Issue 6: Administrator's remuneration

The Referred Proposal was 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 who conduct external administrations are remunerated for their work from the assets of the company in question. This remuneration is protected by a right of indemnity,[57] which generally has a priority over other debts of the company[58] and is secured by a lien on the company's property.[59]

It is common in practice for an incoming liquidator to reach an agreement with a former administrator about the payment of their respective remuneration out of available corporate assets. 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 right to remuneration of any other person who is subsequently appointed liquidator.

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57 s 443D.
58 s 443E.
59 s 443F.

Any remuneration of an administrator or a liquidator must:

- be reasonable,[60] and
- be approved by creditors or the court.[61]

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.[62] The lien remains in force even after the assets under the administrator's control pass to a 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

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60 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.

61 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* (1998) rec 38, *Rehabilitating large and complex enterprises in financial difficulties* (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, and
- 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 (ss 473(5), 504).

62 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 (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).

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.[63] However, that priority ranks equally with a similar right of the liquidator.[64]

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 a 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

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63 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).

64 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.

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 was:

> 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.

Submissions

Various respondents supported the principle of protecting the remuneration of the administrator. PP6 could act as an incentive to retain the person initially appointed, thereby avoiding the expense of appointing a replacement.

The ACF, while supporting PP6 as a matter of equity and fairness, queried whether this is not already the outcome under the present operation of the law.

The IPA agreed with PP6, but raised some additional matters, to ensure a balanced consideration of the issue:

- PP6 may result in administrators who are removed by creditors for poor performance or a perceived lack of independence being rewarded by payment of their remuneration in priority to a replacement liquidator (though the IPA considered this factor to be counterbalanced by the right of creditors to refuse approval of the administrator's remuneration and the court's power to review the remuneration of administrators[65])

- it may not be reasonable for an administrator to benefit from the work done by the liquidator (though the liquidator may also benefit from work done by the administrator)

65 s 449E(2).

- it has been held that, where funds are insufficient to pay both the administrators' and liquidators' remuneration, the administrators are only entitled to be paid remuneration in relation to those assets of the administration companies that were realised under their administration in accordance with their equitable lien and that 'it would be unconscionable for the administrators to benefit from the fruits of the liquidator's labour'.[66]

The LCA put forward both majority and minority views. The majority view, with which the NSW Law Society Business Law Committee agreed, was that the current provisions for the remuneration of insolvency practitioners work equitably[67] and implementation of PP6 would deter persons from accepting appointment as replacement liquidator. The LCA minority supported PP6.

Advisory Committee recommendation

> **Recommendation 6**
>
> The Corporations Act should not be amended to give the remuneration of the administrator (or deed administrator) priority over that of any replacement liquidator where a company is put into liquidation after an administration (or deed of company arrangement).

This recommendation reverses PP6.

> ***Reasons for recommendation***
>
> The Advisory Committee recognises the importance of ensuring that administrators have some level of assurance that they will be paid for their work. Administrators already have lien and priority rights, as discussed above. However, the Committee is no longer convinced that an additional statutory priority as in PP6 is appropriate.

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66 *ASIC* v *McKenney Consulting Pty Ltd* (2003) 21 ACLC 314 at [41].

67 The respondent cited the principles of incontrovertible benefit and the residual power in the court (s 485(3) as applied to a creditors' voluntary liquidation by s 511(1)(b), or alternatively, s 447A) to alter priorities as the court thinks just if the property recovered is insufficient to satisfy all costs, charges and expenses of the winding up in full.

While PP6 would add to certainty for administrators, and may help ensure that administrators are paid for work already done, there are various contrary considerations:

- the proposed change could be unfair if administrators inflate their costs
- it may be unfair to give an administrator priority for fees incurred when the liquidator has not yet completed the task of liquidating the company
- there may be a disincentive for liquidators to recover assets on behalf of the companies to which they have been appointed if they do not have a reasonable expectation of being paid
- it may displace the equitable principles of 'salvage', which would give the liquidator priority for costs incurred in recovering particular assets. Any modification of PP6 to preserve the doctrine of salvage may be overly complex and, in the event, may not be successful.

In practice, a commercial resolution of the respective claims for remuneration is usually achieved by negotiation between the outgoing administrator and the replacement liquidator. Also, there are various controls over the remuneration of liquidators and administrators,[68] including a right for liquidators to challenge excessive claims for remuneration by administrators[69] and for administrators to make a similar challenge to the remuneration of liquidators.[70]

68 ss 449E (administrators), 499, 504 (liquidators).

69 s 449E(2) (the liquidator would have the right to challenge as an 'officer' of the company and also as a 'creditor' for the amount of the unpaid remuneration).

70 s 504 (the administrator would have the right to challenge as a 'creditor' of the company for the amount of the unpaid remuneration).

4 Liquidation

This chapter considers issues 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 is settled by the company going into liquidation.

The terms of reference raise two questions 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)
- whether 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 was 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.[71] The provisional liquidator has various powers, including to carry on the business of the company.[72]

The remuneration of a provisional liquidator can only be determined by the court.[73]

By contrast, creditors can approve the remuneration of a court-appointed liquidator, with the court determining the matter if the creditors fail to do so.[74] Before creditors make a decision on remuneration, the liquidator must provide them with a report 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.[75]

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[76]
- judges may not be well qualified to work out remuneration.[77]

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71 s 472(2).

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

73 s 473(2).

74 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).

75 s 473(11), (12).

76 Insolvency Practitioners Association Submission on the Exposure Draft of the Corporations Amendment (Insolvency) Bill para 20.2.

If creditors are empowered to determine the remuneration of a provisional liquidator, they could be given the same type of information as is provided to them in the case of remuneration of a liquidator.

Also, the conferral on creditors of a power to determine the remuneration of a provisional liquidator need not exclude the current power of the court to do so.

Advisory Committee provisional position

PP7 was:

> 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.

Submissions

All submissions supported PP7, though the LCA and the NSW Law Society Business Law Committee considered that it should be limited to an insolvent winding up. Those respondents considered that it would be inappropriate to give creditors a role in approving the liquidator's remuneration in a solvent winding up, given that creditors have no economic interest in that remuneration, as they would be paid in full.

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[77] 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:

> 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.

Advisory Committee recommendation

Recommendation 7

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 insolvent 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 for recommendation

Creditors of companies in insolvent liquidation should have the same ability to determine remuneration, whether the person in control of the company is a liquidator or a provisional liquidator.

The recommendation is limited to insolvent liquidations, as creditors have no need to be involved in this matter in a solvent winding up, given that they will be paid in full.

4.1.3 Issue 8: Postal voting by creditors

The Referred Proposal was 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.

Background

Specified matters

The Referred Proposal specifies three matters relating to liquidators:

- remuneration
- the power to compromise debts
- the power to enter into long-term agreements.

The issue of remuneration would apply to all liquidators, whether in a court or voluntary winding up, while the powers to compromise debts and to enter into long-term agreements only apply to court-appointed liquidators.

Remuneration. The determination of the remuneration of a court-appointed liquidator is in the first instance a matter for agreement between the liquidator and the creditors' committee of inspection.[78] 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.[79] 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.[80]

A court-appointed 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.[81]

In a creditors' voluntary winding up, the committee of inspection or, if there is no such committee, the creditors, may fix the liquidator's remuneration.[82] In a members' voluntary winding up, the shareholders by resolution may fix the liquidator's remuneration.[83]

Compromise of debts. A court-appointed 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.[84] The liquidator may unilaterally compromise a lesser amount claimed by the company.

Long-term agreements. A court-appointed liquidator cannot enter into a long-term agreement, such as a lease or a charge, without the approval of the court, the committee of inspection or a resolution of

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78 s 473(3)(a).
79 s 473(3)(b), (4).
80 ss 473(5), (6).
81 s 473(4).
82 s 499(3).
83 s 495(1).
84 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).

creditors.[85] 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.[86] As already indicated, these matters will usually be considered by the committee of inspection (generally constituted in larger liquidations), 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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85 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.

86 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. The requirement for all matters to be determined at 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[87]

- 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 an objection by creditors to dispensing with a physical meeting include:

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87 Compare the arguments for retaining physical meetings for listed public companies in the Advisory Committee report *Shareholder Participation in the Modern Listed Public Company* (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 a 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 was:

> 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).

The discussion paper also asked whether electronic voting should be permitted in addition to postal voting[88] (with the first vote received by the company being the one recorded[89]).

Submissions

Most respondents supported PP8 either in its entirety or subject to qualifications.

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88 The Advisory Committee report *Shareholder Participation in the Modern Listed Public Company* (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).

89 id at para 4.135 and rec 20.

The IPA, while supporting PP8, considered that only one issue should be dealt with at any one time, to prevent confusion.

The CLA agreed with PP8 except in relation to approval of the liquidator's remuneration, where greater scrutiny through a physical meeting is appropriate.

The LCA disagreed with PP8, arguing that:

- current proxy voting procedures are sufficient to enable individual creditors to vote without physically attending the meeting
- creditors' meetings enable creditors to present arguments to other creditors and call liquidators to account
- postal voting would usually result in creditors merely endorsing the recommendations put forward by the liquidator.

There was general support for electronic voting. The LCA and the NSW Law Society Business Law Committee observed that this form of voting was already permissible.

Advisory Committee recommendation

Recommendation 8

A liquidator should have the option to conduct a postal vote on a proposal relating to remuneration.

A court-appointed liquidator should also have the option to conduct a postal vote on a compromise of debts under s 477(2A) or an agreement under s 477(2B).

However:

- a physical meeting should be required if a threshold objection level to a postal vote is reached (say, 5% by number or value of persons entitled to vote)
- if more than one of the specified matters is being voted on, each issue should be set out in a clearly separate proposal and voted on separately.

This recommendation modifies PP8 by including a requirement that matters should be voted on separately.

Reasons for recommendation

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 efficiency benefits of postal voting, including the cost savings, outweigh any concerns about permitting a postal vote, even in the case of a vote on the liquidator’s remuneration.

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.

The Committee acknowledges the view in submissions that electronic voting is already permissible without the need for legislative amendment.

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 transactions that were entered into by the company before the winding up began and that may give an undue advantage to counterparties or beneficiaries of those transactions over other creditors in the distribution of available corporate assets.

Voidable transactions are:

- unfair preferences[90]
- uncommercial transactions[91]
- unreasonable director-related transactions[92]
- transactions obstructing creditors' rights[93]
- unfair loans to the company[94]

that were entered into on behalf of the company, before the winding up began,[95] by various parties including:

- directors or officers prior to a voluntary administration (where the company goes from voluntary administration into liquidation)
- (from 31 December 2007) directors or officers pursuant to a DOCA under which the company has been returned to the control of directors (officer-initiated transactions)[96]
- a receiver or other controller (or a person acting under their authority).

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90 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.

91 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.

92 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.

93 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).

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

95 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.

96 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* (1998), paras 8.1–8.18, rec 51.

However, 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.[97] Also, transactions entered 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.[98]

Action to set aside affected transactions

Where the voidable transaction provisions apply, the liquidator may commence an action against a counterparty or beneficiary of a 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.[99]

A defendant in these proceedings may 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.[100]

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97 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.

98 s 588FE(2A), (2B).

99 s 588FF.

100 Under the assumed solvency defence, a beneficiary need only prove that 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 to a counterparty in relation to unreasonable director-related transactions or unfair loans: s 588FG(2).

Issues

The terms of reference raise two questions 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 (Issue 13)
- whether the assumed solvency defence should be removed for officer-initiated transactions (Issue 9).

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

The Referred Proposal was 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 (removal of the assumed solvency defence) would only be relevant where a company that is subject to a DOCA has entered into officer-initiated transactions and has subsequently gone into liquidation. The proposal did 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 rely on the defence.

Arguments for retaining the assumed solvency defence for officer-initiated transactions 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
- removal of the defence may make it more difficult during the DOCA period for officers to enter into transactions that are designed to assist the company's recovery, given that counterparties may be more reluctant to trade with the company if their transactions could be avoided because of the lack of that defence
- it would be 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 was:

> 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.

Submissions

All respondents supported PP9.

The IPA considered that removing the defence could deter creditors from dealing with the company, hindering the viability of the company.

Advisory Committee recommendation

> **Recommendation 9**
>
> The assumed solvency defence should remain for transactions entered into by officers of a company while the company is under a deed of company arrangement.

Reasons for recommendation

Removal of the assumed solvency defence may make transactions entered into by directors or other officers of a company that is subject to a DOCA too uncertain for the counterparty. Abolition of the defence could also 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[101]
- to apply to the court for authorisation to search for and seize property or books of a company[102] or to examine company officers[103]
- to inquire into the conduct of liquidators[104]
- to cause the accounts of a liquidator to be audited[105]
- to investigate matters referred to in the reports of liquidators[106]
- to initiate proceedings against anyone in breach of the Corporations Act.[107]

In addition:

- applicants for winding up must lodge a notice of the application with ASIC[108]
- a liquidator must lodge with ASIC a preliminary report about the affairs of the company,[109] as well as a report if it appears to the

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101 ss 459P(1)(f), 461–464.
102 s 530C.
103 ss 596A, 596B, para (a) of the definition of 'eligible applicant' in s 9.
104 s 536.
105 s 539.
106 *ASIC Act* s 15.
107 s 1315(1)(a).
108 s 470.
109 s 476.

liquidator that past or present officers, employees or members have committed any offences.[110]

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

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

4.3.2 Issue 10: Replacing a liquidator

The Referred Proposal was 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[111]) or creditors (in a creditors' voluntary winding up[112]) may fill any vacancy in the office of liquidator, which may arise if the previous incumbent ceases to be a registered liquidator,[113] resigns or dies.

The court also has a power to appoint a liquidator to fill a vacancy in either form of voluntary winding up.[114] Only the court may appoint a replacement liquidator in a court winding up.[115] 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.[116]

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.

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110 s 533.
111 s 495(3).
112 s 499(5).
113 s 532(1).
114 s 502.
115 s 473(7).
116 See, for instance, *Federal Court (Corporations) Rules 2000* r 7.2, *Supreme Court (Corporations) Rules 1999* (NSW) r 7.2.

Any provision of this nature should not place an obligation on ASIC to monitor liquidations and apply for replacement liquidators.

Advisory Committee provisional position

PP10 was:

> 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.

Submissions

Most respondents agreed with PP10.

ASIC proposed an alternative approach, whereby it would have an administrative power, without a court application, to replace a liquidator in the stipulated circumstances. ASIC suggested that this would be a quicker, more convenient and less costly procedure than a court application and, therefore, in the interests of creditors.

Advisory Committee recommendation

Recommendation 10

ASIC should have power to replace a liquidator in the event of a vacancy in that office.

This recommendation adopts a different approach from PP10.

Reasons for recommendation

It would be beneficial to confer on ASIC a power to replace a liquidator in the event of a vacancy in that office. Such a power would obviate the need for ASIC to make a court application.

4.3.3 Issue 11: Taking possession of and transferring books

The Referred Proposal was 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.

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[117] in their possession that relate to the company.[118]

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.[119]

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.[120]

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.[121] 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 was 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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117 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).

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

119 s 438C.

120 ss 530A, 530B.

121 *ASIC Act* Part 3 Div 3.

Advisory Committee provisional position

PP11 was:

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

Submissions

Most respondents agreed with PP11.

ASIC favoured an approach under which it would have administrative power to transfer a company's books in the event of a vacancy in the office of the liquidator or administrator without the need to obtain a court order. The CLA and IPA also supported an administrative power for ASIC.

Advisory Committee recommendation

Recommendation 11

ASIC should have power to take possession of and transfer the books of a company in the event of a vacancy in the office of an external administrator.

In addition, an interested party should have the right to apply to the court for directions about the temporary holding of books.

This recommendation adopts a different approach from PP11.

Reasons for recommendation

The key concern is to ensure the security of books of a company in external administration.

For this purpose, ASIC should have power to obtain and transfer the books of a company if there is a vacancy in the office of external administrator (for instance, if the external administrator dies or is no longer registered), to ensure that action is taken promptly.

In addition to the ASIC power, an interested party should be able to apply to the court for directions about the temporary holding of books, given the importance of ensuring the security of books of a company in external administration.

5 Receivers and other controllers

This chapter considers questions about 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 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.[122]

The terms of reference raise questions:

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

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122 Definition of 'controller' in s 9.

Background

Receivers and other controllers are subject to various statutory,[123] as well as general law, requirements when acting on behalf of their appointors. The principal statutory obligations are:

- *sale of assets:* controllers must 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[124]

- *reporting:* controllers must lodge with ASIC accounts showing details of their corporate transactions affecting the relevant corporate assets.[125]

There is no provision for exempting controllers from either of these requirements.

In addition, the courts have various supervisory powers over controllers, for instance, to make orders in relation to the exercise of their duties[126] or their obligation to lodge accounts[127] and to remove a controller for misconduct.[128] A controller can also apply to the court for directions concerning the exercise of his or her powers.[129]

The issue is whether either or both of the principal statutory obligations applicable to controllers are too onerous for those enforcing the type of securities mentioned in the Referred Proposal ('relevant security enforcers'). A bank, or an agent of the bank, which enforces a security over a piece of real property owned by a corporation, would be a controller.

Policy options

Policy options in relation to the sale of assets and reporting by receivers and other controllers include:

- *Option 1:* retain current obligations

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123 Part 5.2.
124 s 420A.
125 s 432.
126 s 423.
127 s 434.
128 s 434A.
129 s 424.

- *Option 2:* retain the sale of assets obligation but exclude the reporting obligation
- *Option 3:* retain the sale of assets obligation but replace the reporting obligation with an obligation to provide information to a relevant party on request
- *Option 4:* exempt relevant security enforcers from both statutory obligations (the Referred Proposal).

Option 1: retain current obligations

The current provisions seek to ensure that controllers are accountable through their reporting obligations and act in a proper manner when selling corporate property, regardless of the number or value of the assets involved.

Option 2: retain the sale of assets obligation but exclude the reporting obligation

A relevant security enforcer would be exempted from the requirement to lodge accounts,[130] though not from the statutory duty when exercising the power of sale. It is arguable that the current reporting requirements unduly increase the cost of a controllership in the case of low value assets (less than $100,000).[131]

In a general report on insolvency (the Harmer Report), the Australian Law Reform Commission (ALRC) considered it 'unnecessarily burdensome to require a receiver who, for example, has taken control of a single item of property constituting only a small part of the total property of a company to comply with the reporting requirements'[132] (though the ALRC report made no recommendation, as the matter was outside its terms of reference).

Option 3: retain the sale of assets obligation but replace the reporting obligation with an obligation to provide information to a relevant party on request

The statutory obligations to report enforcement of a security over a single asset and prepare and provide accounts would arise only on

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130 s 432.

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

132 Australian Law Reform Commission, *General Insolvency Inquiry* (Australian Government Publishing Service, Canberra, 1988) (ALRC 45), vol 1, para 186.

request of a relevant party to the mortgagee or chargee (on payment of a prescribed fee), rather than in every case.

Relevant parties for this purpose would be:

- an external administrator
- another creditor
- ASIC
- the borrower, guarantor or any subsequent registered chargeholder (or any person claiming through them).

The key reporting obligations to ASIC would be removed.

The removal of the obligations to provide accounts and report to ASIC would not affect the obligations of a mortgagee or chargee to act properly and comply with s 420A (duty involved in sale of assets), as well as the common law obligations of a mortgagee or chargee when enforcing a security. The obligations of a mortgagee/chargee in relation to preservation, maintenance and sale (including compliance with appropriate sale processes) should continue to apply.

Option 4: exempt relevant security enforcers from both statutory obligations

This approach 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[133]). Also, relevant security enforcers would not be subject to judicial controls, except in very limited circumstances.[134]

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133 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.

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

Advisory Committee provisional position

PP12 was:

> 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.

Submissions

Most respondents, including the majority view of the LCA, supported Option 1.

However, the AFC supported an amendment along the lines of Option 3, and the minority view of the LCA supported Option 4, to avoid compliance costs in smaller matters. The AFC argued that Option 3 would relieve the chargee of the time and cost involved in preparing and lodging statements of account utilising the ASIC form and better reflect the current commercial practice of reconciling the outcome of repossession and sale of secured assets and advising customers (or external administrators) of that process and outcome.

The LCA recommended the removal of freehold mortgages from the definition of 'charge' in the Act, as compliance with the controllership provisions imposes an unnecessary burden and cost.

Advisory Committee recommendation

Recommendation 12

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 for recommendation

The Advisory Committee is not persuaded that the law should be amended to provide an exemption from either the sale of asset obligation or the reporting obligation of relevant security enforcers.

The current provisions seek to ensure that all controllers are accountable and act properly when selling corporate property: the requirement for controllers to lodge accounts with ASIC ensures that interested parties can obtain information about how the security has been enforced. This right to be informed outweighs any administrative burden on relevant security enforcers in lodging this information.

If relevant security enforcers were not subject to this reporting obligation, they would only be obliged, in relation to any real property securities that they were enforcing, to disclose certain information to the mortgagor under State and Territory real property legislation.[135]

Moreover, it cannot be assumed that a single or low value asset will necessarily constitute a minor part of the assets of the company. A single asset could be significant in any administration, while the proposed monetary amount ($100,000) could be significant in a small administration.

An exemption from the requirement to lodge accounts would deny interested parties access to this information, while providing limited savings, given that the relevant security enforcer would still have to account in some manner to the appointor.

The suggested exemption in the Referred Proposal is arbitrary (in the sense that it imposes a $100,000 limit) and could have adverse consequences (for instance, it may call into question whether s 420A would apply to protect mortgagees in this case).

Other parties searching the company register are entitled to know whether the company's assets are subject to enforcement proceedings.

5.3 Voidable transactions

5.3.1 Context

Transactions by receivers or other controllers[136] as agents of the company after their appointment under a charge, but before the

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[135] 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.

[136] A 'controller' in relation to property of a corporation is defined (s 9) to mean:
- a receiver, or receiver and manager (see ss 90, 416), of that property (defined in ss 9, 416), or

winding up begins, are subject to the voidable transaction provisions.

Voidable transactions are:

- unfair preferences
- uncommercial transactions
- unreasonable director-related transactions
- transactions obstructing creditors' rights
- unfair loans to the company

that were entered into by various parties on behalf of the company before the winding up began.[137] The court has the power to unwind these transactions.

However, some transactions by controllers on behalf of the security holder, even when using proceeds from the sale of corporate assets, are not subject to the unfair preference provisions.[138]

Also, transactions entered into by controllers after the winding up begins are not subject to those provisions.[139]

- 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.

137 Further details are set out in Section 4.2.1.

138 In *Sheahan v Carrier Air Conditioning Pty Ltd* (1997) 189 CLR 407, a majority of the High Court held that, under the terms of the security, the proceeds from the sale of corporate assets became the property of the security holder. Transactions by the controller with those proceeds were not subject to the unfair preference provisions, as they no longer involved corporate assets.

139 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.

5.3.2 Issue 13: Exemption from voidable transaction provisions

The Referred Proposal was 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 kind of transaction at which the Referred Proposal is directed is a payment of commercial necessity made prior to a 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[140] from repossessing goods that are essential to the continuation of the business.

Duties of controllers

Controllers have duties to the parties for whom they act. Unlike administrators and deed administrators, they are not required to act in the general interest of unsecured creditors. Their role is 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[141]

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[140] Parties to a contract for the sale of goods are permitted to specify in the contract the time at which the property in the goods is to be transferred: see, for instance, *Sale of Goods Act 1923* (NSW) s 22. Reservation of title (Romalpa) clauses provide that title to goods does not pass from the seller to the purchaser until they have been paid for.

- they are subject to the supervision of the court.[142]

In addition, receivers or receivers and managers, being officers of the company, are subject to certain statutory duties.[143]

Arguments for an exemption

The Referred Proposal originated from two submissions on the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007.[144]

One submission[145] argued that no transactions entered into by receivers or other controllers acting within their powers should be treated as voidable, 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 certain transactions (given that transactions by the administrator or under the administrator's authority are exempt from the voidable transaction provisions),[146] 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

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141 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.
142 s 423.
143 Principally ss 180–184.
144 Australian Bankers' Association, Henry Davis York.
145 Australian Bankers' Association.
146 The same point was raised by Henry Davis York Submission para 7.4.

- 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 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 could be:

- 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.[147]

Arguments against an exemption

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

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

- an exemption for these transactions may enable unsecured creditors to negotiate a more favourable arrangement for

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147 s 420A.

payment of outstanding debts, contrary to the pari passu principle[148]

- an action for breach of a fiduciary duty or a duty in exercising the power of sale is less likely to succeed than an action to unwind transactions under the voidable transaction provisions.

Policy options

Options for change include:

- *Option 1:* adopt the Referred Proposal to exempt all transactions by receivers and 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 to the receiver's appointor at a significant undervalue

- *Option 3:* only exempt from the voidable transaction provisions a payment by controllers to the supplier of an 'essential service'.[149]

Advisory Committee provisional position

PP13 was:

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

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148 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.

149 As defined in s 600F.

Submissions

Various respondents supported PP13, arguing that:

- it would assist the ongoing trading of the business
- the greater possibility of corporate rescue if receivers can enter into transactions unaffected by the voidable transaction provisions outweighs the possible disadvantage to unsecured creditors.

The support of one of those respondents (Hargovan) was conditional on adoption of the following safeguards:

- clarify that the definition of 'officer' in s 9 (which includes receivers, as well as receivers and managers) applies to Part 2D.1 and that receivers are therefore subject to ss 180-184
- resolve uncertainties about the operation of s 420A (dealing with receivers' and other controllers' power of sale) by:
  - making it clear that it provides an independent new cause of action for borrowers (and possibly guarantors and third parties)
  - stipulating that the provision is a civil penalty provision
  - providing more substantial criminal penalties for breach of the provision.

The LCA majority did not agree that transactions conducted under the authority of a receiver or other controller should be exempted from the voidable transaction provisions. Their view was that unfair preferences are covered by the case law[150] and there should be no exemption for other types of voidable transaction. The LCA minority was of the view that these transactions should be exempted.

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150 In *Sheahan v Carrier Air Conditioning Pty Ltd* (1997) 189 CLR 407, a majority of the High Court held that, under the terms of the security, the proceeds from the sale of corporate assets became the property of the security holder. Transactions by the controller with those proceeds were not subject to the unfair preference provisions, as they no longer involved corporate assets.

The CLA had various reservations about PP13:

- it would exempt the controller from the avoidance provisions in relation to uncommercial/fraudulent transactions (including unfair loans to directors and director benefit transactions), which are essentially a fraud on the company and should not bind the company's creditors
- it could undermine the interests of unsecured creditors.

The same respondent considered that any exemption should be confined to preferences (Policy option 2). It noted that the current law could have the benefit of encouraging secured creditors to appoint an administrator (transactions by whom are not subject to the voidable transaction provisions[151]) rather than a receiver and manager.

Advisory Committee recommendation

Recommendation 13

No exemption from the voidable transaction provisions should be introduced for transactions conducted under the authority of a receiver or other controller.

This recommendation reverses PP13.

Reasons for recommendation

The Committee originally proposed that receivers and other controllers be exempt from the voidable transaction provisions. The Committee no longer holds that view.

While the proposed exemption could provide greater certainty in transactions between receivers or controllers and third parties, the obligation of receivers and controllers is to act in the interests of their appointor secured creditor, rather than creditors generally. The exemption would give an unwarranted protection to transactions entered into between a receiver or controller and a third party.

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151 s 588FE(2A).

6 Information issues in external administration

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

6.1 Provision of information to the public

6.1.1 Overview

The terms of reference raised the following questions relevant to the provision of information about companies in external administration 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 disclose 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 was 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 publish specified information about the affairs of the company. In each case, the information must be published in newspapers.

Public notices relating to insolvency proceedings in court include:

- notice of application for an order that a company be wound up[152]
- notice of an order substituting the plaintiff in an application for a winding up order[153]
- notice of the making of a winding up order and appointment of a liquidator[154]
- notice of appointment of a provisional liquidator[155]
- notice of application by a liquidator for special leave to distribute a surplus.[156]

Other public notices relating to external administration include:

- notice that a company has appointed an administrator[157]
- notice of creditor meetings in a voluntary administration[158]
- notice to submit particulars of a debt or claim[159]
- notice to submit a formal proof of debts or claims.[160]

These public disclosure obligations are in addition to obligations on external administrators to communicate directly with known creditors (discussed at 6.2.2: Issue 16).

Policy considerations

Overview

The Referred Proposal raises the issue of whether, or to what extent, the Internet should replace print media as the required means of

152 Harmonised Corporations Rules: rule 5.6(2)(b).
153 rule 5.10(2)(b)(i).
154 rule 5.11(4)(b).
155 rule 6.2(4)(b).
156 rule 7.9(3)(b).
157 s 450A.
158 s 439A(3)(b), Corp Reg 5.6.14A.
159 Corp Reg 5.6.39.
160 Corp Reg 5.6.48.

publishing the range of public notices arising from external administrations. The Referred Proposal refers to public insolvency notices, but the discussion in this report has been extended to public notices relating to all forms of external administration. This review does not consider the scope or content of these notices.

Options for amending the current requirements for notification to the public of aspects of external administrations 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).[161]

Each of the options contemplates some use of the Internet for public notices. This could involve publication on a general website, administered by ASIC or some other body, for these notices.

A requirement that all public notices be lodged on a website for external administrations would ensure that they are publicly accessible at one location. External administrators or other notice-givers could also choose to place public notices on other relevant websites (for instance, the website of the company under external administration).

Examples of this kind of website are the Company Alert System administered by ASIC or the proposed single national online register of personal property security interests.[162]

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161 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.

162 *Personal Property Securities Bill 2008 Commentary* (May 2008), Chapter 10: Personal Property Securities Register.

Consideration of options

The first option, to retain the current print disclosure requirements and add Internet disclosure requirements, 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 or the associated costs.

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

The third option, by relying on the Internet as the forum for public disclosure, may result in the greatest cost saving.

An argument for placing greater emphasis on the Internet as the preferred forum for public disclosure is that print notices, even if they appear in a number of newspapers, are generally available only 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 mandatory method for publishing public notices related to external administrations, for instance:

- step 1: a combination of print and Internet publication of 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 on a designated website for these public notices.

Advisory Committee provisional position

PP14 was:

> 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.

Submissions

Most respondents supported PP14 as a way of improving the speed of notification and reducing administrative costs and the possibility of misplaced notices.

ASIC supported in principle the concept of Internet disclosure of all public notices connected with external administration. It suggested that this could best be achieved by means of a corporate insolvency register, accessible through the current ASIC website, rather than by setting up a separate website. This approach would integrate public insolvency notices with other corporate information on the existing ASIC public registers.

ASIC also suggested that, in the transitional phase, a standard statement could be published daily in the public notices section of major newspapers along the following lines:

> For public insolvency notices, refer to
> www.asic.gov.au/insolvencynotices.

The IPA, while supporting use of the Internet, suggested that consideration be given to a tender process to determine who should administer the website. Also, it considered that clear times and steps should be established for the transition from print to the Internet.

Advisory Committee recommendation

Recommendation 14

There should be a staged move, administered by ASIC, of public notices relating to external administration from the print media to an ASIC website.

Reasons for recommendation

Electronic publication is potentially a more effective way than print publication to bring information to the notice of people who may have an interest in the fact that a company is in external administration. It should afford savings in cost and time. An appropriate transitional period would be sensible, to allow interested parties time to adjust.

ASIC is an obvious body to develop and administer a website for this purpose. Access to relevant information on the website should be free of charge, given the general public interest in that information.

In addition to the mandatory disclosure obligations in force from time to time, it will also remain open to external administrators to choose to publish notifications in the print media or on other websites (for instance, the website of the company under external administration). Furthermore, media reports will continue to be a source of information to the public.

The means that ASIC adopts to implement the staged move could include appropriate advertisements or notices in newspapers.

6.1.3 Issue 15: Exemption from publication

The Referred Proposal was 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

A company in external administration that changes its name[163] during, or six months prior to, the external administration must disclose its former name as well as its current name on public documents, for the period of the administration or any subsequent liquidation.[164]

A deed administrator has the right to apply to the court for an exemption from this disclosure requirement.[165] The court could grant the exemption:[166]

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163 A liquidator, administrator, deed administrator, managing controller or receiver of a company can lodge an application with ASIC to change the 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.

164 s 161A (introduced by the *Corporations Amendment (Insolvency) Act 2007* and operative from July 2008)). This provision implements a recommendation of the Advisory Committee: *Corporate Voluntary Administration* (1998) rec 60.

165 s 161A(6).

> 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.[167]

The question raised by the Referred Proposal was 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 would not affect the separate requirement to disclose in public documents that a company is in external administration.[168]

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 include:

- the disclosure requirement may adversely affect the ability of those persons to sell the business of a company that is in external administration[169]
- an exemption from disclosure may assist the chances of a better return for existing 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 people who may deal with the company in the future 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.

A contrary view is that existing and future creditors are entitled to be informed of any former name under which the company has traded.

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166 It is noted that, due to an apparent drafting error, the court's power to grant an exemption from disclosure is expressed in s 161A(3) to relate to a company under administration, rather than one subject to a deed of company arrangement. Nevertheless, it may be that the court, pursuant to its general discretionary power (s 447A), could modify the law and grant an exemption in relation to a company subject to a deed of company arrangement.

167 s 161A(7).

168 See, for instance, s 450E.

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

This information may better enable them to assess the company's past performance.

Another view is that an exemption may be more justifiable 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.

Advisory Committee provisional position

PP15 was:

> 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.

Submissions

Most respondents supported PP15, given that the discretion in the court would protect the public interest and the interests of those dealing with the company.

The NSW Law Society Business Law Committee suggested that ASIC should be notified of any application to the court.

The majority view of the LCA was that any power to grant an exemption from the disclosure requirement should rest with ASIC, not the court, with ASIC's decision to be reviewable by the Administrative Appeals Tribunal.

Advisory Committee recommendation

Recommendation 15

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 requirement for a company to publish its former name on public documents. In exercising its discretion on such an application, the court could take into account the possible prejudice to relevant parties, including past creditors and persons who may deal with the company in the future.

Applicants for relief from the disclosure requirement should notify ASIC of the application.

Reasons for recommendation

The Advisory Committee does not see why the right to apply to the court for an exemption from the rule requiring a company to publish its former name on public documents should be confined to only some external administrators, given that the court can consider the particular circumstances of each case in deciding whether an exemption is justified.

While it would be appropriate in many instances to require the company to publish its former name on public documents, the requirement for court approval would ensure that the exemption is only granted where justified by the particular circumstances.

The Advisory Committee is not persuaded that it would be more appropriate for ASIC rather than the court to have the exemption power.

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.[170] Similar obligations of personal notification apply in liquidations.[171] In some circumstances, deed administrators may also need to communicate with creditors.[172]

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

6.2.2 Issue 16: Electronic communication with creditors

The Referred Proposal was that:

> The new mechanism for electronic communication with creditors [operative from 31 December 2007] 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

The 'new mechanism for electronic communication with creditors' mentioned in the Referred Proposal, and now found in s 600G of the Corporations Act, permits creditors to 'opt in' to receive electronic communications from administrators, deed administrators or liquidators (external administrators) in that:

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170 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].

171 For instance, ss 496(2), 497(1), (2).

172 For instance, s 445F. Also, Recommendation 4 (Section 3.2.2) is that the deed administrator should be required in some circumstances to notify creditors of a breach of a DOCA.

- 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.[173]

Issues with the creditor 'opt in' approach

Steps to enable external administrators to communicate with creditors electronically may increase efficiency and save time and administrative costs, with a consequential increase in funds available for distribution to creditors.[174]

However, in its submission on the Exposure Draft of the Insolvency Bill, the Insolvency Practitioners Association argued that an 'opt in' system for electronic communication with creditors may not be fully effective, in that:

- there is little 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.[175]

Also, electronic addresses such as email are often person-specific and an entity may not receive an email if the relevant person leaves the organization.[176]

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

[174] 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: *Re Ansett Australia Ltd and Mentha* (2002) 40 ACSR 419 at [16].

[175] para 21.3.

Advisory Committee provisional position

PP16 was:

> 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.
>
> 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.
>
> 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.

Submissions

All respondents supported the principle of electronic communication, as it would increase efficiency and save time and cost.

The IPA put forward an approach (which the minority of the LCA supported) that would modify PP16 in some respects. Under the IPA approach:

- an external administrator would have the right, but not the obligation, to make reports available online through the same website as would be used in implementing PP14 (this element is the same as PP16)
- an external administrator who chooses this online approach would be required to send a one page notification informing creditors of the availability of the document online and a telephone number to request a paper version (this element has the same effect as PP16)

[176] ibid.

- creditors would be notified each time a document is available online (this contrasts with PP16, which provides that creditors are to be notified, either electronically or by mail, only if they have previously so requested).

The majority of the LCA, as well as the NSW Law Society Business Law Committee, did not support moving beyond the 'opt-in' approach under s 600G of the Corporations Act. They considered that a move to an 'opt-out' regime (as in PP16) could be contemplated after a review of how s 600G worked in practice.

Advisory Committee recommendation

Recommendation 16

External administrators should be permitted to advise in their first notification to creditors that all further notices to creditors and other documents relevant to the external administration will be published on a designated website.

That first notification should also indicate that a creditor may choose to register:

- to be notified electronically when new material is placed on the website(s), or
- to receive by mail, free of charge, a printed version of these further notices and other documents.

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 for recommendation

This approach is consistent with the view of the Advisory Committee in its report *Rehabilitating large and complex enterprises in financial difficulties* (2004):

> 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.[177]

The recommendation seeks to reduce the administrative burden, and thereby the cost, of an external administration, while ensuring that creditors are properly notified. External administrators would only have to give further notification, electronically or in print, to creditors who so requested, whereas the effect of s 600G of the Corporations Act is that external administrators must provide printed documents to all creditors except for those who have elected to receive them electronically.

177 para 2.5.