Chapter 3

The role and duties of liquidators and administrators in the insolvency process in Australia

3.1 This chapter examines the role and duties of liquidators and administrators in the insolvency process in Australia. It is divided into the following eleven sections:

- the role of an administrator (paragraphs 3.4–3.6);
- the role of a receiver (paragraphs 3.7–3.9);
- the role of a liquidator (paragraph 3.10);
- secured and unsecured creditors (paragraphs 3.11–3.12);
- the voluntary administration process (paragraphs 3.13–3.27);
- deeds of company arrangement (paragraphs 3.28–3.41);
- the process of a receivership (paragraphs 3.42–3.48);
- creditors' scheme of arrangement (paragraphs 3.49–3.50);
- the liquidation or 'winding up' process (paragraphs 3.51–3.83);
- the treatment of employees' entitlements (paragraphs 3.84–3.102); and
- the 'fit and proper' requirement of the *Corporations Act 2001* (paragraphs 3.103–3.117).

The administration of companies in financial difficulty

3.2 A company is classified as being solvent if, and only if, it is able to pay all of its debts as and when they become due and payable (subsection 95A(1)), otherwise the company is insolvent (subsection 95A(2)). Where a company is in financial difficulty and it appears that it may become insolvent (or already is insolvent), there are several forms of external administration available whereby control of the company's affairs is taken from the company's directors and put into external hands. These forms of external administration include:

- voluntary administration;
- receivership;
- creditors' scheme of arrangement; and
- winding up.

3.3 'Winding up' is the terminal mode in the life cycle of a company, which results in the closure of its operations. Portions of the business may be resurrected

after sale by the liquidator. The other three forms of external administration may avoid the finality of this outcome.[1]

The role of an administrator—an overview

3.4 The role of an administrator is to take control of a company and its property and to investigate its affairs. An administrator must be a registered liquidator. The administrator is required to hold an initial meeting of creditors at which creditors may consider whether a committee of creditors should be appointed to liaise with the administrator, in order to ensure that all creditors are kept fully informed. During this meeting, creditors may also resolve to replace the administrator.

3.5 The administrator is also required to call a second meeting of creditors. Prior to this meeting, the administrator must provide a statement to creditors outlining the administrator's opinion in relation to what should happen to the company, the basis of that opinion and any other information necessary for the creditors to make an informed decision. At this second meeting, the creditors are able to decide if:

- the company should be wound up;
- the administration should end; or
- the company should execute a deed of company arrangement (section 439C of the *Corporations Act 2001*[2]).

3.6 If creditors resolve to either enter into a deed of company arrangement or to wind up a company, the administrator may become the administrator of the deed of company arrangement or the liquidator, depending on the wishes of creditors (section 446A).[3]

The role of a receiver—an overview

3.7 A receiver is generally appointed by a secured creditor to:

- collect and sell enough of a company's assets to repay a debt owed to the secured creditor; and
- pay out the money collected in the order required by law.

3.8 Receivers must also report to the Australian Securities and Investments Commission (ASIC) any possible offences or other irregularities that they find.

3.9 A receiver's primary duty is to the company's secured creditor. The main duty owed to unsecured creditors is an obligation to take reasonable care to sell property

---

1 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, p. 122.

2 All references to sections in this chapter refer to the *Corporations Act 2001 (Cth)*.

3 The Treasury, *Submission 18*, pp 4–5.

for not less than its market value or, if there is no market value, the best price reasonably obtainable.[4]

The role of a liquidator—an overview

3.10 In ordinary circumstances, the role of a liquidator is to take control of, and to wind up, a corporation. The liquidator may:

- collect, protect and realise the company's assets;
- investigate and report to creditors about the corporation's affairs, including voidable transactions and claims against the corporation's officers;
- enquire into the failure of the corporation and possible offences by people involved in the corporation and report to ASIC;
- distribute the proceeds of realisation of assets including processing claims by creditors—first to secured creditors, then priority creditors (including employees), followed by unsecured creditors; and
- apply for deregistration of the company on completion of the liquidation.[5]

Secured and unsecured creditors

3.11 A creditor of a company is a person who is owed money by that company. Usually, a creditor is owed money because they have provided goods or services, or made loans to the company. An employee who is owed money for unpaid wages and other entitlements is also a creditor. Generally, there are two basic categories of creditor:

- a secured creditor is someone who has a charge, such as a mortgage, over some or all of the company's assets to secure a debt owed by the company. In particular, lenders usually require a charge over company assets when they provide a loan; and
- an unsecured creditor is a creditor who does not have a charge over the company's assets.

3.12 Employees are a special class of unsecured creditor. Employees' outstanding entitlements are usually paid in priority to the claims of other unsecured creditors.[6]

---

4 Australian Securities and Investments Commission, *Receivership: A Guide for Creditors*, December 2008, p. 2.

5 The Treasury, *Submission 18*, p. 4.

6 Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008, p. 1.

Voluntary administration

3.13 Voluntary administration was introduced in 1993 to provide an inexpensive procedure capable of being implemented swiftly (part 5.3A of the *Corporations Act*). Voluntary administration provides several options to creditors for dealing with a financially troubled company. Some possible outcomes of voluntary administration include:

- ending the voluntary administration and returning the company to the directors' control;
- the company resuming operations but with a deferred or reduced debt burden under a deed of company arrangement approved by creditors;
- a secured creditor exercises its rights to appoint a receiver to obtain repayment of its debt by disposal of company assets; or
- the creditors vote to wind up the company and appoint a liquidator.

3.14 Voluntary administration seeks to maximise the chances of an insolvent company surviving or, if it (or parts of it) cannot be saved, to achieve a better return for creditors and members than would result from an immediate winding up of the company (section 435A). [7]

Commencement and effect of voluntary administration

3.15 Voluntary administration is usually initiated by the company itself when directors resolve that:

- in their opinion the company is insolvent or likely to become insolvent at some future time; and
- an administrator of the company should be appointed (subsection 436A(1)).

3.16 While a company is under administration, the administrator has control of the company's property and business (section 437A). The powers of other corporate officers, including directors, are suspended during the administration and may not be exercised except with the written approval of the administrator (subsection 437C(1)). However, company officers are not removed from their offices by the appointment of an administrator (subsection 437C(2)).

3.17 It is also possible, although much less common, for a voluntary administrator to be appointed by a liquidator of a company (section 436B) or by a substantial chargee: that is, a secured creditor who is entitled to enforce a charge over the whole, or substantially the whole, of the company's property (section 436C). A liquidator may appoint themselves (or a partner, employee or associate) as administrator with the leave of the court or where the appointment is approved by resolution at a meeting of

---

7 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, p. 123.

creditors. If, under administration, the company then executes a deed of company arrangement, the court may stay or terminate the winding up. Winding up (liquidation) is discussed in further detail below.

3.18 An administrator must notify secured creditors of their appointment as soon as practicable, but no later than the next business day (subsection 450A(3)). Soon after an administrator's appointment it is possible for a substantial chargee to enforce its charge, usually by the appointment of a receiver (section 441A). An administrator's powers are subject to those of the chargee and its receiver: if a substantial chargee decides to enforce its charge it effectively supplants the administration (subsection 442D(1)). However, if they wish to override the powers of the administrator, a substantial chargee must enforce its charge in relation to all of the relevant property—it does not have the option of appointing a receiver to only a part of the relevant property (subsection 441A(1)(b)). This is generally referred to as the 'all or nothing' rule, which is justified on the basis that a company's assets should be administered either by a receiver or an administrator free of the problems that may arise in a system of divided or competing control of the assets. Receivership is discussed in further detail below.

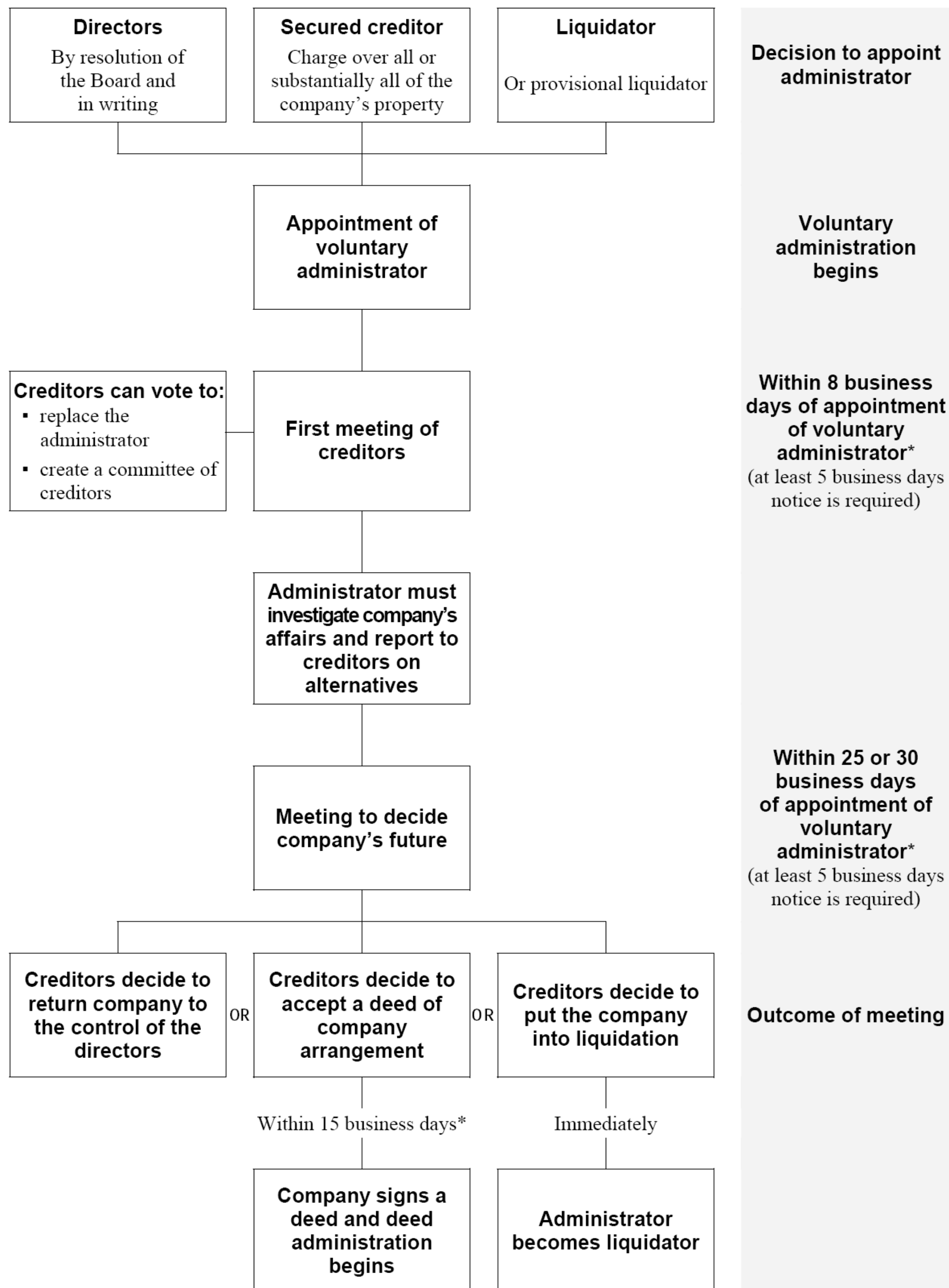
3.19 If there is no substantial chargee or it does not enforce its charge, during the period of administration there is a general moratorium upon actions or proceedings against the company and its property by creditors and owners or lessors of property used by the company (sections 440A–440D and 440F). This moratorium is intended to provide a period for investigation and collective assessment of options without a general scramble for individual recovery. This generally means that while a company is in voluntary administration:

- unsecured creditors cannot begin, continue or enforce their claims against the company without the administrator's consent or the court's permission;
- owners of property (other than perishable property) used or occupied by the company, or people who lease such property to the company, cannot recover their property;
- except in limited circumstances (for example, where there is a substantial chargee as discussed above), secured creditors cannot enforce their charge over company property;
- a court application to put the company in liquidation cannot be commenced; and
- a creditor holding a personal guarantee from the company's director or other person cannot act under the personal guarantee without the court's consent. [8]

---

8 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 123–126; and Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008.

Chart 3.1: The Voluntary Administration Process[9]



* Unless the court allows an extension of time.

---

9 Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008, p. 2.

First creditors' meeting

3.20 As soon as practicable, an administrator must investigate the company's business, property and financial circumstances (section 438A), and within strict but not inflexible time limits, convene two meetings of creditors to take decisions in relation to the administration. An administrator must convene the first meeting within eight business days after the voluntary administration begins. In convening the meeting an administrator must:

- give written notice of the meeting to as many of the company's creditors as reasonably practical; and
- publish a notice of the meeting in an appropriate newspaper (section 436E).

3.21 The administrator must send to creditors, with the notice of first meeting, declarations about any relationships they may have, or indemnities they have been given, to allow creditors to consider the administrator's independence and make an informed decision about whether they want to replace them with another administrator of the creditors' choice.

3.22 At this meeting:

- a determination is made about whether to appoint a committee of creditors to consult with (but not give directions to) the administrator (sections 436E–436F); and
- creditors may replace the administrator with a qualified person of their choosing (subsection 436E(4)).

3.23 The role of a committee of creditors is to consult with the administrator about matters relevant to the administration and receive and consider reports from the administrator. The committee can also require the administrator to report to them about the administration. It may also approve the administrator's fees.

Proposals to nominate an alternative administrator

3.24 A creditor who wishes to nominate an alternative administrator must approach a registered liquidator before the meeting and get a written consent from that person that they would be prepared to act as administrator. The proposed alternative administrator should give to the meeting declarations about any relationships they may have, or indemnities they have been given. The administrator will only be replaced if the resolution to replace them is passed by the creditors at the meeting.[10]

---

10 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 123–126; and Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008.

Second creditors' meeting—deciding the company's future

3.25 It is the second meeting of creditors where the major decisions in relation to the administration are made. This meeting is usually held about five weeks after an administrator is appointed, although this is extended to six weeks at Christmas and Easter. An administrator must give written notice to creditors and advertise this meeting in the same way as for the first meeting. With the notice of meeting, an administrator must:

- provide a report to creditors about the company's business, property, affairs and financial circumstances;
- provide a statement setting out their opinion (and reasons for their opinion) about whether it would be in the creditors' interests for the company to execute a deed of company arrangement, for the administration to end, or for the company to be wound up; and
- if a deed of company arrangement is proposed, provide a statement setting out details of the proposed deed (section 439A).

3.26 At this meeting the creditors may resolve that:

- the administration should end (and the company be returned to the control of its directors)—a rare occurrence;
- the company be wound up; or
- the company execute a deed of company arrangement (section 439C).

3.27 If creditors resolve that the company should be wound up, the administrator becomes the liquidator unless creditors vote at the second meeting to appoint a different liquidator of their choice. The liquidation proceeds as a creditors' voluntary liquidation.[11] Winding up (liquidation) is discussed in further detail below.

Deeds of company arrangement

3.28 Deeds of company arrangement are sometimes referred to as 'moratorium deeds' (in which a company is granted an extended period in which to repay its debts in full) or 'compromise deeds' (under which creditors agree to receive less than their full debt). If creditors vote for a proposal that the company enter a deed of company arrangement, the company must sign the deed within 15 business days of the creditors' meeting, unless the court allows a longer time. (If this does not happen, the company will automatically go into liquidation, with the administrator becoming the liquidator.) The deed administrator is usually the administrator of the company, unless the creditors appoint someone else at the meeting (sections 444A–444B).

---

11 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 123–126; and Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008.

3.29 It is the role of the deed administrator to ensure the company (or others who have made commitments under the deed) carries through these commitments. The extent of the deed administrator's ongoing role is set out in the deed. Creditors also have the right when a deed of company arrangement is proposed and considered at the second meeting to negotiate consequences of failure to meet such deadlines into the terms of the deed.

Distribution of funds

3.30 The order in which creditor claims are paid depends on the terms of the deed. Sometimes the deed proposal is for creditor claims to be paid in the same priority as in a liquidation. Other times, a different priority is proposed. However, the deed must ensure employee entitlements are paid in priority to other unsecured creditors unless the eligible employees agree by a majority in both number and value to vary their priority. Treatment of employees' entitlements is discussed in further detail below.

Potential impact on small unsecured creditors

3.31 A deed of company arrangement binds all unsecured creditors (even if they voted against the proposal). The deed also binds secured creditors and owners and lessors of property used by the company who voted for the deed, and the company and its officers and shareholders (sections 444D and 444G).[12] Professor Bob Baxt and Mr Jason Harris suggest that:

> …the freedom and flexibility offered by the deed of company arrangement procedure can have disastrous consequences for small unsecured creditors. It is not hard to imagine that a deed of company arrangement may be supported by large creditors because it unduly favours their interests at the expense of small creditors. It must be remembered that s 444D binds all unsecured creditors to the effect of the deed, meaning that there is the potential for smaller creditors to be locked in to an unfair proposal (particularly given that voting at creditors' meetings is heavily influenced by the value of debt owed to each creditor, meaning that small unsecured creditors may have very little opportunity to influence the process of outcomes of voluntary administration).[13]

3.32 However, Professor Baxt and Mr Harris contend that section 445D, whereby the court can terminate a deed of company arrangement, 'provides an effective protection measure to ensure that deeds do not operate outside the purposes of Part 5.3A.'[14] The objects clause for Part 5.3A specifies that the object of the Part is to

---

12 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 123–126; and Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008.

13 R. Baxt and J. Harris, *Corporations Legislation 2009*, Thomson Reuters, Pyrmont, 2009, pp 521–522.

14 R. Baxt and J. Harris, *Corporations Legislation 2009*, Thomson Reuters, Pyrmont, 2009, p. 522.

provide for the business, property and affairs of an insolvent company to be administered in a way that:

- maximises the chances of the company, or as much as possible of its business, continuing in existence; or
- if it is not possible for the company or its business to continue in existence—results in a better return for the company's creditors and members than would result from an immediate winding up of the company (section 435A).

Conclusion of a deed of company arrangement

3.33 A deed may come to an end because the obligations under the deed have all been fulfilled and the creditors have been paid. The deed may also provide that the company will go into liquidation if the deed terminates due to certain conditions being met. Another way for the deed to end is if the deed administrator calls a meeting of creditors, and creditors vote to end the deed. This may occur because it appears unlikely that the terms of the deed can be fulfilled. At the same time, creditors may be asked to vote to put the company into liquidation.

3.34 As noted above, the deed may also be terminated if a creditor, the company, ASIC or any other interested person applies to the court and the court is satisfied that:

- creditors were provided false and misleading information on which the decision to accept the deed proposal was made;
- the administrator's report left out information that was material to the decision to accept the deed proposal;
- the deed cannot proceed without undue delay or injustice; or
- the deed is unfair or discriminatory to the interests of one or more creditors or against the interests of creditors as a whole (section 445D).

3.35 If the court terminates the deed as a result of such an application, the company automatically goes into liquidation.[15]

Administrators' fees

3.36 An administrator is entitled to receive remuneration as determined:

- by agreement between the administrator and the committee of creditors (if any); or
- by resolution of the company's creditors; or
- if there is no such agreement or resolution—by the court (subsection 449E(1)).

---

15 Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008.

3.37 Generally, an administrator's fees will be paid from available assets, before any payments are made to creditors. Apart from fees, administrators are entitled to reimbursement for out-of-pocket expenses that have arisen in carrying out the administration. This reimbursement does not usually require approval.

3.38 To be effective, a resolution of the company's creditors specifying an administrator's remuneration must deal exclusively with remuneration of the administrator, i.e. the resolution must not be bundled with any other resolution (subsection 449E(1B)).

3.39 Before remuneration is determined by agreement between an administrator and a committee of creditors, or by resolution of the company's creditors, the administrator must prepare a report setting out:

- such matters as will enable the committee of creditors (or the company's creditors) to make an informed assessment as to whether the proposed remuneration is reasonable;
- a summary description of the major tasks performed, or likely to be performed, by the administrator; and
- the costs associated with each of those major tasks.

3.40 The administrator must give a copy of the report to each member of the committee of creditors at the same time as the member is notified of the relevant meeting of the committee, or where the remuneration is determined by resolution of the company's creditors, at the same time as the creditor is notified of the relevant meeting of creditors (subsections 449E(5–7)).

3.41 A court may, on the application of ASIC, the administrator, or an officer, member or creditor of the company, review the administrator's remuneration and confirm, increase or reduce it (section 449E).[16]

Receivership

3.42 Securities given by companies to lenders usually grant the lender the right, when default occurs, to appoint a person to take possession and control either of a particular asset (or group of assets), or the whole of the property and undertaking of the company. This person is known as a receiver and is empowered to deal with these assets in such a way as is necessary to obtain repayment of the debt that is the subject of the security. An overview of the role of a receiver is provided at paragraphs 3.7–3.9 above. While receivership does not necessarily result in the winding up of the company, it is a common outcome because the remaining assets will usually be inadequate to repay unsecured debts. This is particularly so given the commercially

---

16 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 123–126; and Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Creditors*, December 2008.

traumatic circumstances of receivership and its negative effect on the company's business operations.[17]

3.43 The security (or charge) held by a secured creditor under which the appointment of a receiver is made may comprise:

- a fixed charge over particular assets of the company (e.g. land, plant and equipment); and/or
- a floating charge over assets that are used and disposed of in the course of normal trading operations (e.g. debtors, cash and stock). [18]

Distribution of funds

3.44 The money from the realisation (sale) of these assets must be distributed by the receiver as follows:

- money from the sale of fixed charge assets is paid to the secured creditor after the costs and fees of the receiver in collecting this money have been paid; and
- money from the sale of floating charge assets is paid out as follows: first, the receiver's costs and fees in collecting this money; second, certain priority claims, including employee entitlements (if the liability for these has not been transferred to a new owner); and, third, repayment of the secured creditor's debt.

3.45 Any funds that are left over are paid to the company or its other external administrator if one has been appointed. (It is possible for a company in receivership to also be in provisional liquidation, liquidation, voluntary administration or subject to a deed of company arrangement.)

3.46 The receiver has no obligation to pay any other unsecured creditors for outstanding pre-appointment debts. [19]

Receivers' fees

3.47 As noted above, the receiver is generally entitled to be paid their fees from the money realised from the charged assets. How the fees are calculated is usually set out in the charge document and appointment document. Unsecured creditors have no role in setting or approving the receiver's fees. However, ASIC, a liquidator, voluntary administrator or deed administrator may apply to the court for the receiver's remuneration to be reviewed (section 425).

---

17 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 126–127.

18 Australian Securities and Investments Commission, *Receivership: A Guide for Creditors*, December 2008, pp 1–5.

19 Australian Securities and Investments Commission, *Receivership: A Guide for Creditors*, December 2008.

Conclusion of a receivership

3.48 A receivership usually ends when the receiver has collected and sold enough assets to repay the secured creditor, completed all their receivership duties and paid their receivership liabilities. Generally, the receiver resigns or is discharged by the secured creditor. Unless another external administrator has been appointed, full control of the company and any remaining assets goes back to the directors. Although, as noted above, while receivership does not necessarily result in the winding up of the company, it is a common outcome because the remaining assets will usually be inadequate to repay unsecured debts. [20]

Creditors' scheme of arrangement

3.49 A creditors' scheme of arrangement is another device that may be used by a company in financial difficulty in an effort to prevent the company from facing the prospect of being wound up. Under a creditors' scheme of arrangement a company facing the prospect of insolvency may restructure its debts through a compromise of creditors' claims similar to that which may be reached under a deed of company arrangement.

3.50 A creditors' scheme of arrangement is initiated by application to the court for an order that a meeting of creditors be convened and for approval of an explanatory statement to be sent to creditors with the notice of meeting (sections 411 and 412). The meeting (or separate meetings where creditors interests are different in relation to the proposed arrangement) considers the proposed scheme. A scheme binds creditors only if it is approved by a majority of creditors in each class who between them hold at least 75 per cent of the total debt of those creditors who are present in person or by proxy at the meeting. Furthermore, the compromise (i.e. the scheme of arrangement) must also be approved by the court (subsection 411(4)). The creditors' scheme of arrangement option was never common and has now been eclipsed by the voluntary administration procedure which is generally regarded as being subject to less formality, delay and expense and greater flexibility of outcome.[21]

Winding up (liquidation)

3.51 Winding up is the process leading to the liquidation of a company and termination of its registration and existence. The purpose of liquidation of an insolvent company is to have an independent and suitably qualified person (the liquidator) take control of the company so that its affairs can be wound up in an orderly and fair way for the benefit of all creditors.

---

20 Australian Securities and Investments Commission, *Receivership: A Guide for Creditors*, December 2008.

21 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, p. 130.

3.52 Under Australian law there are three types of winding up—members' voluntary (this can only be used by solvent companies), creditors' voluntary, and compulsory.

Members' voluntary winding up

3.53 As noted above, members' voluntary winding up can only be used by solvent companies. The directors are required to make a declaration to the effect that the company is capable of paying its debts in full within a period of 12 months. The members of the company decide who will be appointed as liquidator and what their remuneration will be, subject to the court's ability, upon an application being made, to review a liquidator's remuneration.

Creditors' voluntary winding up

3.54 Creditors' voluntary winding up is the most common type of liquidation and is used where a company is insolvent. A company may enter a creditors' voluntary winding up where:

- as noted above, creditors vote for liquidation following a voluntary administration or a terminated deed of company arrangement; or
- an insolvent company's shareholders resolve to liquidate the company and appoint a liquidator.

Compulsory winding up

3.55 Compulsory winding up is effected by an order of the court. It most commonly arises where a creditor petitions the court to have a company wound up on grounds of insolvency, relying on failure of the company to comply with a demand for repayment of a debt (section 459A). The liquidator is appointed by the court and is an officer of the court.

Effect of winding up on company officers and creditors

3.56 In any form of winding up, while a company is being wound up a person cannot perform or exercise, and must not purport to perform or exercise, a function or power as an officer of the company (section 471A(1)). Powers with respect to the company and its property vest in the liquidator who may carry on the business of the company so far as is necessary for the beneficial disposal or winding up of the business (section 477). It is important to note that a winding up order does not affect the rights of secured creditors to realise or otherwise deal with the security (section 471C). However, a winding up order can have significant effects on

unsecured creditors because legal proceedings may then only be brought against the company with the leave of the court.[22]

Distribution of funds

3.57 After a liquidator has realised the assets of a company, the resulting funds are used to pay creditors. The general rule is that all debts and claims proved in winding up rank equally and, if the property of the company is insufficient to meet them in full, they must be paid proportionally (section 555). However, there are exceptions to this general rule. Firstly, as the winding up order does not affect the rights of secured creditors, the funds available for distribution to other creditors are determined after enforcement of their securities. Generally, the order in which remaining funds are distributed is:

- costs and expenses of the liquidation, including liquidators' fees; then
- outstanding employee wages and superannuation; then
- outstanding employee leave of absence (including annual leave, sick leave—where applicable—and long service leave); then
- employee retrenchment pay; and finally
- unsecured creditors.

3.58 Each category is paid in full before the next category is paid. If there are insufficient funds to pay a category in full, the available funds are paid on a pro rata basis (and the next category or categories will be paid nothing).[23]

3.59 As a liquidator's primary duty is to all of the company's creditors it has generally been held that all shareholders' claims rank behind creditors' claims and therefore shareholders are unlikely to receive any funds in an insolvent liquidation unless they also have a claim as a creditor. However, a decision of the High Court in *Sons of Gwalia v Margaretic*[24] determined that certain compensation claims by shareholders against a company are not subordinated below the claims of other creditors. At the time of writing, the Corporations Amendment (Sons of Gwalia) Bill 2010 is before Parliament and seeks to reverse the effect of the High Court's decision. Therefore, if the bill is passed, it would return the law to a situation where all claims

---

22 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 127–130; The Treasury, *Submission 18*, p. 4; and Australian Securities and Investments Commission, *Liquidation: A Guide for Creditors*, December 2008.

23 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 127–130; and Australian Securities and Investments Commission, *Liquidation: A Guide for Creditors*, December 2008.

24 *Sons of Gwalia Ltd v Margaretic* (2007) 232 ALR 232.

against an insolvent company from shareholders would rank equally and be postponed until all other creditors' claims are paid.[25]

Creditors' meetings

3.60 In both types of insolvent winding up, the liquidator is generally not required to call a creditors' meeting unless a matter requires creditor approval. In a compulsory winding up, the only exception is if creditors pass a resolution requiring a creditors' meeting to be called, or at least one-tenth in value of all the creditors request the liquidator in writing to do so. However, it is unusual for this to happen, as those who make the request or pass the resolution must pay the costs of calling and holding the meeting.

3.61 In a creditors' voluntary winding up, the liquidator must hold an annual meeting of creditors or lodge a report with ASIC on the progress in the administration. If they choose not to hold the meeting, the liquidator must tell creditors that the report has been prepared and provide them with a copy if asked. The report must set out:

- an account of the liquidator's acts and dealings and the conduct of the winding up in the preceding year;
- a summary of the tasks yet to be done in the liquidation; and
- an estimate of when the liquidation is expected to be finalised.

3.62 In a creditors' voluntary winding up, the liquidator must also hold a joint meeting of the creditors and members at the end of the winding up. Creditors can require the liquidator to call a creditors' meeting at other times, the same as in a court liquidation, as long as they pay the associated costs.

3.63 In both types of winding up, a meeting may need to be convened by the liquidator to determine their remuneration.

Committees of inspection

3.64 The liquidator may also ask creditors if they wish to appoint a committee of inspection and, if so, who will represent the creditors on the committee. A committee of inspection assists the liquidator, approves fees and, in limited circumstances, approves the use of some of the liquidator's powers, on behalf of all the creditors. Committee meetings can be arranged at short notice, which allows the liquidator to obtain quickly the committee's views on urgent matters. Shareholders may also be members of the committee.

3.65 Creditors in both types of insolvent liquidation can request that the liquidator call separate meetings of shareholders and creditors to decide whether a committee of inspection should be appointed and, if so, who will represent the shareholders and creditors on the committee.

---

25 Corporations Amendment (Sons of Gwalia) Bill 2010, *Explanatory Memorandum*, p. 6.

3.66 A committee of inspection acts by a majority in number of its members present at a meeting, but it can only act if a majority of its members attend. A liquidator must consider any directions given by the committee of inspection, but is not bound to follow them. [26]

Creditors' rights

3.67 In addition to rights involving meetings and the distribution of funds discussed above, the other rights of unsecured creditors include the right to:

- receive written reports about the liquidation;
- inspect certain books of the liquidator;
- inform the liquidator about their knowledge of matters relevant to the affairs of the company in liquidation; and
- complain to ASIC about the liquidator's conduct in connection with their duties.

3.68 Creditors can also apply to the court if they are dissatisfied with an act, omission or decision of a liquidator. This includes if a creditor seeks:

- to challenge a liquidator's decision not to admit a proof of debt or claim, either for voting or dividend purposes; and
- a review of the liquidator's fees, in certain circumstances.

3.69 If a company fails to meet its obligations under a charge (e.g. mortgage), a secured creditor can appoint an independent and suitably qualified person (a receiver) to take control of and realise some or all of the charged assets, in order to repay the secured creditor's debt. This right continues after the company goes into liquidation. Receivership is discussed in detail above.

3.70 Another option available to a secured creditor is to ask the liquidator to deal with the secured assets for them and account to them for the proceeds and costs of collecting and selling those assets.

3.71 A secured creditor is entitled to vote at creditors' meetings for the amount the company owes them that exceeds the amount they are likely to receive from realisation of the charged assets. The secured creditor can participate in any distribution of funds to unsecured creditors on a similar basis. [27]

---

26 Australian Securities and Investments Commission, *Liquidation: A Guide for Creditors*, December 2008.

27 P. Redmond, *Companies and Securities Law: Commentaries and Materials*, Fifth Edition, Thomson Reuters, Pyrmont, 2009, pp 127–130; The Treasury, *Submission 18*, p. 4; and Australian Securities and Investments Commission, *Liquidation: A Guide for Creditors*, December 2008.

Liquidators' fees

3.72 A liquidator is entitled to be paid for the work carried out on the liquidation, but only if there are assets available. The liquidator cannot be paid until the amount of fees has been approved by one of the methods set out in the Corporations Act.

3.73 In a compulsory winding up, the amount of fees is approved by:

- agreement with a committee of inspection (if there is one); or
- a resolution passed at a creditors' meeting; or
- the court.

3.74 A liquidator must try to get approval by each of these methods, in turn.

3.75 In a creditors' voluntary liquidation, a committee of inspection or creditors may approve the fees.

3.76 If no fees have been approved in a compulsory winding up or a creditors' voluntary winding up, the liquidator may draw fees to a maximum of $5000 where they have called a meeting of creditors but not obtained approval for their fees because the meeting did not have a quorum.

3.77 The court has the power to review the amount of fees approved in a similar way to those of an administrator or receiver (sections 473 and 504).

3.78 If creditors are asked to approve fees either at a meeting of a committee of inspection or in a general meeting of creditors, the liquidator must provide creditors, at the same time as the notice of the meeting, a report that contains sufficient information to assess whether the fees claimed are reasonable. The report should set out:

- a description of the major tasks performed;
- the costs of completing these tasks; and
- such other information that will assist in assessing the reasonableness of the fees claimed.

3.79 Apart from fees, the liquidator will also be entitled to reimbursement for out-of-pocket expenses that have arisen in carrying out the liquidation. This reimbursement does not require committee, creditor or court approval. However, creditors have a right to know what funds were spent on these costs and why they were spent. [28]

---

28 Australian Securities and Investments Commission, *Liquidation: A Guide for Creditors*, December 2008.

Conclusion of the winding up

3.80 A winding up effectively comes to an end when the liquidator has realised and distributed all the company's available property and made their report to ASIC.

3.81 As noted above, in a creditors' voluntary winding up, the liquidator must hold a final joint meeting of the creditors and members to give an account of how the liquidation has been conducted and how company property has been disposed of. After the final meeting is held, the company is automatically deregistered by ASIC three months after a notice of the holding of the meeting was lodged.

3.82 In a compulsory winding up, the liquidator is not required to hold a final meeting of creditors. After the liquidator decides that the company's affairs are fully wound up, they may:

- seek an order for release from the court;
- seek an order for release and that ASIC deregister the company; or
- if there are insufficient assets to obtain a court order for the company's deregistration, request that ASIC deregister the company.

3.83 A company ceases to exist after it has been deregistered.[29]

Treatment of employees' entitlements

Voluntary administration

3.84 If a voluntary administrator continues to operate the business, they must pay out of the assets available to them ongoing wages for services provided and other employee entitlements that arise after the date of their appointment. These payments are treated as an expense of the voluntary administration.

3.85 The appointment of an administrator does not automatically terminate the employment of the company's employees. As a result, unless the administrator adopts the employment contracts or enters into new contracts of employment with employees, they are not personally liable for any employee entitlements that arise during administration.

3.86 As voluntary administration is an interim form of external administration, employee entitlements that arose prior to voluntary administration are not usually paid during voluntary administration. How and when these employee entitlements are paid depends on the option passed at the second creditors' meeting (i.e. company returned to directors, a deed of company arrangement, or liquidation).

---

29 Australian Securities and Investments Commission, *Liquidation: A Guide for Creditors*, December 2008.

Company is returned to directors' control

3.87 If the company is returned to the directors, the directors will be responsible for ensuring that the company pays outstanding entitlements as they fall due. As noted above, it is only in very rare circumstances that creditors will resolve to return the company to the control of its directors.

Deed of company arrangement

3.88 If creditors approve a deed of company arrangement, the priority in which outstanding employee entitlements are paid depends on the terms of the deed. A deed of company arrangement must ensure that employees' entitlements have the same priority as in a liquidation unless the eligible employees agree by a majority in both number and value to vary this priority. This means that unless a variation to priority is agreed to, in a deed of company arrangement employees have the right, if there are funds left over after payment of the fees and expenses of the voluntary administrator and deed administrator, to be paid their outstanding entitlements in priority to other unsecured creditors.

3.89 Priority employee entitlements are grouped into classes and paid in the following order:

- outstanding wages and superannuation; then
- outstanding leave of absence (including annual leave and sick leave, where applicable, and long service leave); and then
- retrenchment pay.

3.90 Each class is paid in full before the next class is paid. If there are insufficient funds to pay a class in full, the available funds are paid on a pro rata basis (and the next class or classes will be paid nothing).

3.91 If a deed proposal seeks to vary the priority for employee entitlements, the administrator must call a meeting of eligible employees giving at least five business days notice of the meeting. They must give to eligible employees at the same time as the notice of meeting a statement setting out:

- their opinion about whether the proposed variation would result in the same or better outcome for employees than if the company went into liquidation;
- their reasons for this opinion; and
- any other information to help them make an informed decision about varying the priority.[30]

30 Australian Securities and Investments Commission, *Voluntary Administration: A Guide for Employees*, April 2010.

Receivership

3.92 As in a voluntary administration, if a receiver continues to operate the business, they must pay out of the company assets available to them, ongoing employee wages for services provided and other employee entitlements that arise after the date of appointment. These payments are treated as an expense of the receivership.

3.93 The appointment of a receiver and manager does not automatically terminate the employment of the company's employees. As a result, unless the receiver adopts the employment contracts or enters into new contracts of employment with employees, they are not personally liable for any employee entitlements that arise during the receivership.

3.94 If the company's business is sold by the receiver as a going concern, it may be that most, if not all, of the company's employees will keep their jobs. In this case, it is usual for the new owner to take over the company's liability for outstanding employee entitlements.

3.95 If there are insufficient funds to pay all creditors in full, the money from the realisation of assets must be distributed as follows:

- money from the sale of fixed charge assets is paid to the secured creditor after the costs and fees of the receiver in collecting this money have been paid; and
- money from the sale of floating charge assets is paid out as follows:
  - the receiver's costs and fees in collecting this money; then
  - certain priority claims, including employee entitlements (if the liability for these hasn't been transferred to a new owner); and then
  - repayment of the secured creditor's debt.

3.96 In both cases, any funds left over are paid to the company or its external administrator, if one has been appointed.

3.97 If employee entitlements are to be paid by the receiver under a floating charge, the payments must be made in the order outlined in paragraphs 3.88 and 3.89.[31]

Winding up (liquidation)

3.98 In most cases, the winding up of a company terminates the employment of employees.

3.99 Employees have the right, if there are funds left over after payment of the fees and expenses of the liquidator, to be paid their outstanding entitlements in priority to

31 Australian Securities and Investments Commission, *Receivership: A Guide for Employees*, April 2010.

other unsecured creditors. In a similar way to what occurs under voluntary administration and receivership, priority employee entitlements are grouped into classes and paid in the order outlined in paragraphs 3.88 and 3.89.

3.100 Employees may also be entitled to make a claim against the General Employee Entitlements and Redundancy Scheme (GEERS). GEERS is administered by the Department of Education, Employment and Workplace Relations. It is a basic payment scheme designed to assist employees whose employment has been terminated due to the liquidation or bankruptcy of their employer.

3.101 If the liquidator continues to operate the business for a short period to help in the winding up, employee entitlements accruing during this period (on terms agreed with the liquidator) are paid out of available assets as a cost of the winding up and before other outstanding employee entitlements.

3.102 If a committee of inspection is formed employees can nominate a representative to be on this committee and have a say in matters that may impact on their interests. As noted above, a committee of inspection is formed to assist the liquidator, approve their fees and, in limited circumstances, approve the use of some of their powers. [32]

Duties and responsibilities of a liquidator and the 'fit and proper' provisions of the Corporations Act

3.103 In the winding up of a company a liquidator owes fiduciary duties to the company, its creditors and members. In addition to these fiduciary duties, liquidators owe other more specific duties as outlined in the Corporations Act and in case law.

Fiduciary duties

3.104 Relevant statute and case law stipulates that, as a fiduciary, liquidators must:

- act honestly.
- avoid conflicts of interest—that is, a liquidator must not permit their personal interests to conflict with those to whom a duty is owed. This obligation applies in a number of ways. For example, a liquidator must not profit from their position, either directly or indirectly, except by way of remuneration for work done (section 182). Furthermore, a liquidator is not at liberty to make contracts with the company.
- act impartially—that is, a liquidator must not favour anyone and must not act as the agent of any group.

32 Australian Securities and Investments Commission, *Liquidation: A Guide for Employees*, January 2008.

Duties of care and skill

3.105 As professionals, high standards are required of liquidators in the carrying out of their tasks. For example, a liquidator should complete the administration of a company within a reasonable time and without protracting the liquidation where there is no reason to do so. A liquidator may be in breach of duty if they do not seek the advice of professionals in areas in which they are not qualified, for example, a solicitor in respect of a legal issues or a valuer regarding the value of property.

3.106 A liquidator is required to act with a reasonable degree of care and skill and liquidators can be liable at common law for failure to exercise due care and skill in performing their duties. Furthermore, as an officer of the company, a liquidator can be liable under section 180, which requires liquidators (and other officers) to exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:

- were a director or officer of a corporation in the corporation's circumstances; and
- occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.

Other duties

3.107 Other duties owed by liquidators include:

- a duty to exercise discretion—that is, while liquidators are entitled to seek advice and appoint agents, they must not delegate the exercise of their professional judgment and discretion;
- a duty not to make improper use of inside information to gain an advantage (section 183);
- a duty to ascertain and take possession of assets;
- a duty to preserve assets;
- a duty to realise assets;
- a duty to lodge a notice of appointment with ASIC and to register for GST;
- a duty to keep records and accounts;
- a duty to report and investigate;
- a duty to settle list of contributories; and
- a duty to ascertain liabilities.[33]

---

33 M. Murray, *Keay's Insolvency: Personal and Corporate Law and Practice*, Sixth Edition, Lawbook Co., Pyrmont, 2008, pp 258–262.

The 'fit and proper' provisions in the Corporations Act

3.108 As highlighted above, high standards are required of liquidators in the carrying out of their tasks. Section 1282(2) stipulates that applicants for registration as liquidators will satisfy minimum educational and experience criteria and demonstrate that they are capable of properly performing the duties and functions of a liquidator. In addition to these requirements, ASIC must be satisfied that the applicant 'is otherwise a fit and proper person'.

3.109 Mr Jeffrey Fitzpatrick, Dr Vivienne Brand and Associate Professor Christopher Symes suggest that:

> The fit and proper person requirement aims to ensure that the general community can have confidence that those seeking registration and those currently holding registration as liquidators possess 'sufficient moral integrity and rectitude of character' as to permit them to be entrusted with significant financial responsibility and personal discretionary power. Public trust in the reliability of liquidators is paramount to maintaining market confidence in company operations in Australia.[34]

3.110 Currently, 'fit and proper person' is not defined in the Corporations Act. In *Hughes and Vale Pty Ltd v State of NSW (No 2)* Chief Justice Dixon and Justices McTiernan and Webb stated that the purpose of the fit and proper person test was 'to give the widest scope for judgment and indeed for rejection...it would be unwise to attempt any definition of the matters which may legitimately be inquired into; each case must depend upon its own circumstances'. ASIC's interpretation of 'fit and proper' is consistent with this judgment.[35]

Initial application for registration

3.111 ASIC's Regulatory Guide 186, specifies that for the purposes of section 1282(2) an applicant for registration as a liquidator is 'otherwise a fit and proper person' if ASIC is satisfied that an applicant has honesty, integrity, good reputation and personal solvency—as well as, an overall capability to perform the duties and functions of a liquidator. ASIC considers applicants in view of:

- the fiduciary nature of a liquidator's duties and function;
- the fact that liquidators often have control of very large amounts of money, other property, financial facilities and financial obligations that belong to third parties;
- the need for a liquidator's words and actions to be regarded with complete trust by persons who deal with them;

34 Mr Jeffrey Fitzpatrick, Dr Vivienne Brand and Dr Christopher Symes, *Submission 6*, p. 2.

35 Mr Jeffrey Fitzpatrick, Dr Vivienne Brand and Dr Christopher Symes, *Submission 6*, pp 3–4.

- any criminal records, disqualification order, or pending legal or disciplinary action;
- referees' opinions;
- residency status; and
- if the applicant is a registered trustee, their record and reputation in that role.

3.112 Mr Fitzpatrick, Dr Brand and Associate Professor Symes suggest that:

> Applicants, by their professional conduct, must continually demonstrate that they can maintain the standards expected of their profession. Factors such as timeliness, truthfulness and personal integrity when dealing with clients and professional bodies demonstrate whether an individual applicant possesses the relevant attributes to be a liquidator.[36]

3.113 ASIC considers an applicant is not a fit and proper person to be registered as a liquidator if:

- in the last ten years, the applicant has been convicted of an offence of which one element was dishonesty; or
- the applicant has been found civilly liable for any breach of trust, breach of fiduciary duty, dishonesty, gross negligence or recklessness in the course of their professional duties; or
- the applicant has been convicted of a serious tax offence; or
- the applicant is personally insolvent; or
- the applicant is disqualified from managing a corporation; or
- the applicant cannot satisfy ASIC that they have full mental capacity.

3.114 ASIC also regards favourably current membership of a body—such as the Institute of Chartered Accountants, CPA Australia or the Insolvency Practitioners Association of Australia—that monitors the professional performance of its members and has disciplinary functions because such bodies usually require their members to be fit and proper persons.

Ongoing registration

3.115 In addition to the initial registration provisions, to remain registered with ASIC as a liquidator they must continually perform adequately and properly the duties and functions of a liquidator and remain a fit and proper person. Section 1292(2) provides that ASIC may apply to the Companies Auditors and Liquidators Disciplinary Board (CALDB) to cancel or suspend a liquidator's registration if they are 'otherwise not a fit and proper person to remain registered as a liquidator'.

36 Mr Jeffrey Fitzpatrick, Dr Vivienne Brand and Dr Christopher Symes, *Submission 6*, p. 5.

3.116 To perform adequately and properly the duties and functions of a registered liquidator means that the liquidator must comply with all the obligations applicable to them in their capacity as a liquidator. As noted above, these obligations include general legal requirements to exercise reasonable care, competence and skill, and to perform all liquidator duties with the highest standards of honesty and integrity and the statutory duties of company officers, including discharging duties with care and diligence and good faith.[37]

3.117 The 'fit and proper' provisions are discussed in chapter 7.

37 Mr Jeffrey Fitzpatrick, Dr Vivienne Brand and Dr Christopher Symes, *Submission 6*, pp 5–10.