Receivership/ Administration/Liquidation

What's the difference and how does it affect creditors?

By Karl Hill (right) and Shannon Martin

The appointment of an insolvency practitioner to a debtor usually strikes fear into the hearts of creditors, as it is considered to mark the death of the company with zero return on any outstanding debts. It is true that the appointment of an insolvency practitioner is a real indication that the debtor company is in serious financial trouble. However, as an insolvency specialist it is surprising how many of our clients do not realise that there are some significant differences between liquidations, voluntary administrations and receiverships, and the way that they affect creditors of a financially unstable company.

Receivership – it's all about the bank

The fundamental distinction between receivership and other forms of external administration is that receivers are usually appointed by a secured creditor (such as a bank) for the purpose of ensuring that the secured creditor gets paid. Therefore, a receiver acts only for the benefit of the secured creditor for whom it was appointed and not all creditors (although they are subject to specific duties).

In most instances a receiver will be appointed under the provisions of a security instrument (such as a fixed and floating charge), which specifies the powers of the receiver. Usually, a court order is not required for the appointment of a receiver. Depending on the nature of the security, a receiver may be appointed to simply realise and sell the secured assets, or to also take control of the company from the directors and carry on the business in the name of the insolvent

FAQ'S – WHAT ABOUT THE CREDITOR'S RIGHTS?

Just because a company is under external administration (in whatever form that may be) it doesn't necessarily mean that creditors have no rights or options. The rights and remedies that creditors may have vary substantially depending on whether the company is in liquidation, voluntary administration or receivership. The following contains the answers to frequently asked questions about creditors' rights, remedies and obligations in each of the forms of administration:

Retention of title

Q: Can I recover my goods from the company which are covered by a retention of title clause in the agreement?

Receivership: Yes, provided that the creditors' rights are not compromised by the security.

Administration: No, unless:

- the goods are perishable; or
- you have commenced enforcing your rights prior to administration; or
- the administrator has consented.

An administrator must not sell goods subject to retention of title claims without a creditor's consent or they must account to the creditor for the sale of those goods.

Liquidation: Yes

Registering caveat

Q: Can I register a caveat against the company's real property which is charged under the agreement?

Receivership: Yes

Administration: Yes, but not without the:

- administrator's consent; or
- leave of the Court.

Liquidation: Yes

Commencing or continuing legal proceedings

Q: Can I commence or continue recovery proceedings for the debt owed by the company?

Receivership: Yes

Administration: Yes, but not without the:

- administrator's consent; or
- leave of the Court.

Liquidation: Yes

Recovery against guarantors

Q: Can I take action to recover the debt owed by the company from the guarantors?

Receivership: Yes

Administration: No, you cannot commence recovery action against a director or close relative of the director under a guarantee while the company is in administration, except with leave of the court.

Liquidation: Yes

Preference claims

Q: Can I be pursued for any (alleged) preferential payments received from the company (usually payments received 6 months prior to appointment)?

Receivership: No

Administration: No

Liquidation: Yes, a liquidator can seek repayment of preference payments from creditors.

Insolvent Trading

Q: Can directors be pursued for insolvent trading?

Receivership: No

Administration: No

Liquidation: Yes

The above information should help creditors to understand their basic rights and options, but for specific advice on individual cases speak to an insolvency specialist to determine your true chance of recovery. A specialised knowledge of the intricate differences between receivership, administration and liquidation, together with an appropriately drafted credit agreement and guarantee could produce a recovery result when you might otherwise think all is lost.

company (as receiver and manager). While receivership is obviously not a good sign for unsecured creditors, it is not necessarily terminal for the company.

At a practical level however, it is not unusual for an administrator or a liquidator to be subsequently appointed to represent the interests of unsecured creditors while the company is in receivership.

Voluntary Administration – maybe it can be saved

When a company is placed into administration it is either insolvent or on the brink of insolvency. Administrators are usually appointed by a resolution of the company's directors, although they may also be appointed by a liquidator, secured creditor or the Court.

On a practical level, there are usually two likely outcomes[1] of a voluntary administration which are:

1. strike a deal for the company to enter into a deed of company arrangement ("DOCA"); or
2. liquidation

The fate of the company is ultimately decided by the creditors at a meeting which is convened approximately 26 days after the administrator's appointment.

The decision of whether the company goes into liquidation or enters into a DOCA is determined by a majority vote of the creditors (based on both number and majority value holding) at this meeting.

A DOCA is, in simple terms, a flexible form of insolvency administration. It may involve the company continuing to trade, the directors or other related parties contributing funds or releasing claims, company debts being refinanced and/or assets of the company being sold. The primary purpose of entering into a DOCA is to achieve a higher return for the company's creditors than they would receive in a liquidation.

Liquidation – it's dead

Once a company has been placed in liquidation (voluntarily or by order of the Court) the prognosis is usually fatal. The role of a liquidator in its purest form is to:

1. realise all of the company's assets (turn them into cash); and
2. distribute these funds among the company's creditors.

Once the liquidator has collected the funds, it will distribute those funds to the company's creditors in the order of priority prescribed by the Corporations Act 2001 (Cth) (subject, of course, to secured interests). The usual outcome is that creditors receive only partial payment of the debt owed to them by the company.

After all of the funds have been distributed among the company's creditors and the affairs of the company are finalised, the liquidator will deregister the company with ASIC. ■

Karl Hill is a Director and Shannon Martin is a Solicitor at Results Legal Solutions.
Shannon also co-authored the April article entitled "Personal guarantees gone wrong".
www.resultslegal.com.au

FOOTNOTES:

1 There is a third outcome – giving control back to the directors. However, this outcome rarely occurs in practice.