



ADVISORY

Insolvency Explained: Voluntary Administration

Introduction – What is a Voluntary Administration (VA)?

The Voluntary Administration process is an alternative to liquidation that provides for the business, property and affairs of an insolvent company to be administered in a way that:

- Maximises the chances of the company continuing in existence; or
- Results in a better return for the company's creditors and members than would result from an immediate winding up of the company.

This is typically done by executing a Deed of Company Arrangement ("DOCA").

VA Appointment

An Administrator, who must be a registered Liquidator, can be appointed by:

- The majority of the company's directors (section 436A of the Act); or
- A Liquidator of the company (section 436B); or
- A person who is entitled to enforce a security interest in the whole or substantially the whole of a company's property (section 436C).

Pursuant to subsection 436A(1) of the Act, the company's directors can appoint an Administrator by passing a resolution to the effect that the **company is insolvent or is likely to become insolvent** at some future time. A Liquidator, pursuant to subsection 436B(1), may by writing appoint an Administrator to the company if they think that the company is insolvent or will become insolvent. In compliance with subsection 436B(2)(f), the Liquidator can appoint himself or herself Administrator if:

- At a meeting the creditors pass a resolution approving the appointment; or
- The appointment is made with leave of the Court.

Pursuant to subsection 436C(1), a person who is entitled to enforce a security interest over the whole or substantially the whole of a company's property may by writing appoint an Administrator to the company, if the security interest has become and is still enforceable.

The appointment of an Administrator cannot be made unless the proposed Administrator has consented in writing to the appointment (section 448A). A person cannot consent to be appointed Administrator unless the person is a Registered Liquidator (section 448B).

In accordance with section 436DA of the Act a person appointed Administrator must as soon as practicable after being appointed make out a **Declaration of Independence, Relevant Relationships and Indemnities** ("DIRRI"). The purpose of the DIRRI is to establish the independence of the appointee. In accordance with subsection 436DA(3), the Administrator must circulate a copy of the DIRRI to creditors when he gives notice of the first meeting of creditors.

First Creditors Meeting

Pursuant to subsection 436E(1) of the Act, the Administrator must convene the first meeting of creditors, to be held within eight (8) business days after the administration begins. The purpose of the meeting is to consider:

- Whether or not to appoint a Committee of Creditors; and/or
- To replace the Administrator.

The functions of a Committee of Creditors as per subsection 436F(1), are to consult with the Administrator and to receive and consider reports from the Administrator.



The Committee cannot give directions to the Administrator (subsection 436F(2)) except to require the Administrator to report to the Committee (subsection 436F(3)). Furthermore, a Committee of Creditors can approve the remuneration of the Administrator (subsection 449E(1)).

Administration Outcomes: Second Creditors Meeting

In accordance with subsection 439A(1) of the Act, the Administrator must convene a second meeting of creditors, such meeting to be held within five (5) business days before or within five (5) business days after, the end of the convening period, which is normally twenty (20) business days beginning on the day after the Administration began. Attached to the notice of meeting will be a copy of the Administrator's Section 439A report. The purpose of the meeting is to:

- Decide upon the future of the company by passing a resolution for the company to adopt one of the normal outcomes of the administration set out in subsection 435C(2), which are that:
 - The company executes a Deed of Company Arrangement ("DOCA"); or
 - The Administration should end; or
 - The company be wound up.
- Determine the remuneration of the Administrator, if it has not already been dealt with by a Committee of Creditors.

Alternatively, and pursuant to subsection 439B(2), creditors can resolve to adjourn the meeting from time to time for a period not to exceed forty-five (45) business days from the date of the second meeting.

In circumstances where it is proposed that employees will surrender their priority status under a DOCA that they would otherwise be entitled to pursuant to sections 556, 560 and 561, then it may be necessary, pursuant to section 444DA, for a separate meeting of eligible employees to be convened in order to pass a resolution approving the priority adjustment. This is most relevant where employees agree to accept payment of their outstanding entitlements in the ordinary course of their employment rather than having them paid out in full under the DOCA.

When convening the second meeting, the Administrator is **required to prepare a comprehensive report** to creditors (pursuant to subsection 439A(4) of the Act) that:

- Details the results of their investigation into the business, property, affairs and financial circumstances of the company.
- Sets out the Administrator's opinions and the reasons for those opinions on each of the alternative courses of action set out above.
- Provides such other information as will enable creditors to make an informed decision in relation to the potential options regarding the future of the Company.
- Includes a statement setting out the details of and DOCA that has been propounded.

Pursuant to Corporations Regulation 5.6.19, a resolution put to the **vote at a meeting** must be decided by majority on the voices (or on a show of hands) unless a poll is demanded. Subregulation 5.6.21(2) states that a resolution is carried under a poll if **a majority in number and value** of creditors present vote in favour of the resolution. Conversely, subregulation 5.6.21(3) states that a resolution is not carried under a poll, if a majority in number and a majority in value of creditors present vote against the resolution.

If a resolution is neither carried nor lost, then regulation 5.6.21(4) gives the chairperson the power to determine the outcome by exercising a casting vote either for or against the motion. If the chairperson declines to exercise a casting vote, or votes against the resolution, then the resolution will be lost.

In the event creditors **resolve to wind up the company**, then pursuant to subsections 446A(1) and 446A(2) of the Act, the company is taken to have passed a resolution under section 491 of the Act that the company has been wound up voluntarily.

If creditors resolve to wind up the company, then pursuant to subsection 499(2A)(a), creditors can seek to appoint a person to be Liquidator for the purpose of winding up the company. If no such appointment is made, then pursuant to subsection 499(2A)(b), the Administrator will automatically become Liquidator of the company.



In the event creditors **resolve that the company executes a DOCA**, then pursuant to subsection 444B(2) of the Act, the DOCA must be executed within fifteen (15) business days after the end of the meeting of creditors, or such further period as the Court allows on an application made within that period.

In the event creditors resolve to **bring the administration to an end**, then control of the company simply reverts to the directors.

Administrator Role and Powers

In accordance with section 437A of the Act, while a company is under administration, the Administrator:

- Has control of the company's business, property and affairs.
- May carry on the company's business and manage its property & affairs; and
- May terminate or dispose of all or part of the company's business or property; and
- May perform any function, and exercise any power, that the company or any of its officers could perform or exercise if the company was not in administration.

Section 437B states that when performing a function or exercising a power, an Administrator is taken to be acting as the agent of the company.

Pursuant to section 438A, an Administrator must investigate the company's business, property, affairs and financial circumstances and form an opinion about whether it is in the interests of the company's creditors for either the company to execute a DOCA, or for the administration to end, or for the company to be wound up.

Section 442A, sets out the additional powers of an Administrator, which comprise:

- Removing from office a director of the company;
- Appointing a person as a director;
- Executing a document, bringing or defending proceedings, or doing anything else in the company's name or on its behalf;
- Whatever else is necessary for the purposes of Part 5.3A.

An Administrator has the power to **carry on the business of a company**.

However, the Administrator will only do so if they can be satisfied that the continuation of trading is in the interests of creditors. The reasons that would support the continuation of trading are:

- The ability of the company to generate a positive cash flow;
- To maximise the realisable value of assets such as stock;
- To facilitate the sale of the company's business;
- To enable a DOCA to be propounded in the expectation that the return under the DOCA will be greater than if the company was wound up;
- The availability of fixed assets to cover trade on debts and expenses.

Pursuant to section 443A, an Administrator is **personally liable** for debts he or she incurs in the performance or exercise of his or her functions and powers. Section 443D gives the Administrator an entitlement to be indemnified out of the company's property for debts, liabilities, damages or losses sustained for which they become liable. The indemnity extends to the remuneration of the Administrator.

The **remuneration of an Administrator** is normally calculated on a time basis using hourly rates set by their firm. The actual costs will depend upon the circumstances and complexity of the administration and can only be drawn down once approved. Pursuant to section 449E of the Act, the Administrator's remuneration can be determined;

- By agreement between the Administrator and the Committee of Creditors (if any); or
- By resolution of creditors; or
- If there is no agreement or resolution, then by order of the Court.

The remuneration of the Administrator would normally be determined at the second meeting of creditors or at any adjournment of that meeting, unless of course the remuneration has already been dealt with by a Committee of Creditors, assuming of course one is in existence.

VA Effect on Director and Members

Pursuant to section 437C of the Act, while a company is under administration, company officers cannot perform or exercise a function or power unless the Administrator has provided written approval for the person to so act.

Following the commencement of the administration, each director must deliver to the Administrator all of the company's books and records in their possession (subsection 438B(1)) and attend upon the Administrator providing such information about the affairs of the company as the Administrator reasonably requires (subsection 438B(3)).

Furthermore, in compliance with subsection 438B(2), the directors must, within five (5) business days after the administration began or such longer period as the Administrator allows, give to the Administrator a statement about the business, property, affairs and financial circumstances of the company.

In so far as members are concerned, pursuant to section 437F, a transfer of shares made after the administration began is void unless either the Administrator gives written consent and any conditions attaching thereto are satisfied, or the Court makes an order authorising the transfer.

Pursuant to section 440J of the Act, during the administration of a company, a guarantee of a liability of a company cannot be enforced against a director of a company or a relative or spouse of a director, except with leave of the Court and in accordance with such terms (if any) as the Court imposes.

VA Effect on Creditors

Section 440D of the Act provides that during the period of the administration, there is a general stay of proceedings against the company or in relation to any of its property. Proceedings cannot be commenced or proceeded with except, with either the written consent of the Administrator or with leave of the Court.

If a creditor is entitled to enforce a security interest in the whole or substantially the whole of the company's property, then pursuant to section 441A, the creditor is able to enforce that interest either before or during the "decision period", which is defined in the Act as the period of thirteen (13) business days after receipt of notice of the Administrator's appointment.

Furthermore, pursuant to section 440C, the owner or lessor of property that is used or occupied by, or is in possession of the company, cannot take possession of the property or otherwise recover it except with the Administrator's written consent or with the leave of the Court.

If a winding up application has been filed, then an Administrator can still be appointed. In compliance with subsection 440A(2), the Court is to adjourn the hearing of an application to wind up a company already in administration, if the Court is satisfied that the continuation of the administration is in the interest of creditors. In our experience, there will need to be evidence put before the Court that will lead the Court to conclude there is a real likelihood that a DOCA will be propounded and that the return under the proposed DOCA will be greater than if the company was wound up. If that cannot be done, then it is likely that the Court will order the winding up of the company in which case the administration ends.

Conclusion – The Main Benefits of a VA

The benefits of a company entering into an Administration include the following:

- Allows immediate action to be taken and sets a fixed time frame for dealing with the issues;
- Control of the company is given to an independent person;
- Prevents unsecured creditors, owners and lessors of property from taking action which may adversely affect the value of a company's business and assets;
- Allows a company and its creditors to consider the merits of a compromise arrangement which may maximise the return to creditors; and
- Enables directors in certain circumstances to avoid personal liability for company debts except for debts that have been personally guaranteed.

Directors of companies that are insolvent or are likely to become insolvent should seek immediate professional advice in relation to their specific circumstances. The procedure normally requires consultation and certain investigative work before implementation, particularly when the intention is to carry on the business of the company or where a secured creditor is in existence.