



Liquidation

Who is a creditor?

You are a creditor if the company owes you money. You may be owed money because you:

- supplied goods or services to the company
- made loans to the company
- paid for goods or services that you have not received
- are an employee owed money for unpaid wages and other entitlements.

A 'contingent creditor' is owed money by the company if a certain event occurs (e.g. if they succeed in a legal claim against the company).

Creditors might be secured or unsecured:

- A secured creditor holds a security interest, such as a mortgage, in some or all the company's assets, to secure a debt owed by the company.
- An unsecured creditor does not hold a security interest in the company's assets.

Employees are a special category or class of unsecured creditor. In a liquidation, outstanding employee entitlements are paid before the claims of other unsecured creditors.



The purpose of liquidation

The liquidation of an insolvent company allows an independent registered liquidator (the liquidator) to take control of the company so its affairs can be wound up in an orderly and fair way to benefit creditors.

There are two types of insolvent liquidation:

- creditors' voluntary liquidation
- court liquidation.

The most common type is a creditors' voluntary liquidation, which begins when:

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

In a court liquidation, a liquidator is appointed by the court to wind up a company following an application (usually by a creditor). Directors, shareholders and Australian Securities and Investments Commission (ASIC) can also make a winding-up application to the court.

After a company goes into liquidation, unsecured creditors cannot commence or continue legal action against the company, unless the court permits.

The liquidator's role

Liquidators have a duty to all company creditors. Their role is to:

- protect, collect and sell the company's assets
- investigate and report to creditors about the company's affairs, including:
 - unfair preferences (payments made to certain creditors over others) that may be recoverable
 - uncommercial transactions that may be set aside
 - possible claims against the company's officers (including insolvent trading)
 - creditor-defeating dispositions, including illegal phoenix activity
- inquire into the failure of the company – and possible offences by people involved with the company – and report to ASIC
- distribute money from the collection and sale of assets after payment of the costs of the liquidation, including the liquidator's fees (subject to the rights of any secured creditor) – first to priority creditors, including employees, and then to unsecured creditors.

Except for lodging documents and reports required under the Corporations Act 2001 (Corporations Act), a liquidator is not required to incur an expense for



the winding up unless there are enough assets to pay their costs.

If the company does not have enough assets, one or more creditors may agree to reimburse a liquidator's costs and expenses to undertake investigations and act to recover further assets. If additional assets are recovered, the liquidator or a creditor can apply to the court to compensate the creditor for funding the liquidator's recovery action. Compensation is usually paid before other creditors are paid.

If a liquidator suspects that people involved with the company may have committed offences, and the liquidation has no or insufficient assets for the liquidator to be paid for their work to further investigate, the liquidator can apply to ASIC for funding to carry out a further investigation into the allegations and report to ASIC.

Recoveries from creditors

A liquidator can recover, for the benefit of all creditors, certain payments the company made to individual creditors (known as 'unfair preferences') in the six months before the start of the liquidation.

A creditor receives an unfair preference if, during the six months before liquidation, the company is insolvent and the creditor suspects (or ought to suspect) the company is insolvent and receives payment of their debt (or part of it) ahead of other creditors.

To be an unfair preference, the payment must put the creditor receiving it in a better position in the winding up than other unsecured creditors.

Not all payments from the company to a creditor in the six months before liquidation are unfair preferences. The Corporations Act provides various defences to an unfair preference claim.

If a liquidator seeks to recover a payment that has been made to you, the liquidator should provide you with reasons and evidence to establish that claim. You may wish to obtain independent legal advice on the merits of the liquidator's claim before repaying any money.

Committee of inspection

A committee of inspection may be formed to assist and advise the liquidator in both a court liquidation and creditors' voluntary liquidation. The committee of inspection also:

- monitors the conduct of the liquidator
- may approve certain steps in the liquidation
- may give directions to the liquidator.

The liquidator must have regard to, but is not always required to comply with, such directions.

The committee may be formed by resolution passed at any meeting



of creditors called for that purpose. All creditors are entitled to stand for committee membership. Members appointed to the committee of inspection represent the interests of all creditors.

If a creditor is a company, the creditor can nominate, in writing, an individual to represent it on the committee.

A committee of inspection has various powers and functions, including to:

- approve the liquidator's remuneration
- direct the liquidator to convene a creditors' meeting
- request the liquidator to give information, provide a report or produce a document
- obtain specialist advice or assistance (with prior approval of the liquidator or court)

A committee of inspection can determine its own procedures and exercise its powers through resolutions passed at meetings of the committee. A resolution is passed by a majority in number of members present at a meeting. The committee of inspection can only act if a majority of its members attend.

Approval of liquidator's fees

A liquidator is entitled to be paid for the necessary work they properly perform. Their fees will usually be paid from available assets before any payments

are made to creditors. If there are no – or only limited assets – the liquidator is sometimes not paid (or only partially paid) for the work they do. The liquidator may arrange for a third party to contribute to their fees.

A liquidator is also entitled to ask for approval to pay their estimated future fees (for work yet to be done). Usually this is requested to allow the liquidator to continue doing work up to a certain point in time (e.g. to achieve a particular outcome) or to the completion of the liquidation.

The fees cannot be paid until the amount has been approved by creditors, a committee of inspection or the court. The liquidator can also put a proposal to creditors to approve their fees without holding a meeting.

If fees are not approved by the relevant decision-making body, the liquidator is entitled to receive reasonable fees up to a specified maximum (indexed annually).

If you are asked to approve fees at a general meeting of creditors, at a meeting of a committee of inspection, or by a proposal put to creditors without a meeting, the liquidator must give you a report with sufficient information to help you assess whether the requested fees are reasonable.

If you do not think the fees are reasonable, raise your concerns with the liquidator.



If fees are approved and you wish to challenge the decision, you can apply to the court for a review of the fees. You may wish to seek your own legal advice about this.

Apart from fees, the liquidator is entitled to reimbursement for out-of-pocket expenses. This reimbursement may require creditor, committee of inspection or court approval.

Distribution of money

If there are funds left over after paying the liquidators' costs and priority creditors, including employees, the liquidator will pay unsecured creditors a dividend. Generally, funds are distributed in the following order:

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

Each category must be 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).

Other creditor rights

As well as the various rights involving meetings and participation in dividends, creditors also have a right to:

- inform the liquidator about what they know that is relevant to the company's liquidation
- request the liquidator give information, provide a report or produce a document
- inspect certain books of the liquidator
- appoint a reviewing liquidator
- remove and replace the liquidator by resolution passed at a creditors' meeting
- complain to ASIC or the court about the liquidator's conduct in connection with their duties.

Liquidator's books

Liquidators must keep sufficient books to give a complete and correct record of their administration of the company's affairs. These include minutes of meetings and details of all the receipts and payments for the liquidation.

These books must be available at the liquidator's office for inspection by creditors and shareholders.

Copies of minutes of meetings and detailed lists of receipts and payments, as well as several other documents, must also be lodged with ASIC. Copies of these



documents may be obtained by searching ASIC Connect for a fee.

Informing the liquidator

If the liquidator suspects anyone connected to the company may have committed an offence, the liquidator must report this to ASIC. Let the liquidator know if you have any information that might assist the liquidator prepare such a report.

These reports are not available for inspection. ASIC reviews these reports and decides whether to take further action, such as banning a person from acting as a company director for a period or charging the person with a criminal offence. ASIC considers a range of factors when deciding what action, if any, to take.

Remove and replace the liquidator

Creditors may remove and replace the liquidator at any time by resolution of creditors passed at a creditors' meeting for which at least five business days' notice is given.

A creditor who wishes to appoint a replacement liquidator must request the current liquidator to convene a meeting. The liquidator is not required to comply if the request is not reasonable. The liquidator must comply with the request if the creditor agrees to pay the cost of calling the meeting, and security for those costs is provided at the liquidator's request.

A creditor who wishes to remove the current liquidator and appoint a replacement liquidator must approach a registered liquidator to get a written consent confirming they would be prepared to act as liquidator of the company. The person must also make a written declaration about any relationships they or their firm may have that might affect their independence to act as liquidator.

Secured creditors' rights

If a company fails to meet its obligations under a security interest (e.g. a charge or a mortgage), a secured creditor can:

- appoint an independent and suitably qualified person (a receiver) to take control of and realise some or all the secured assets in order to repay the secured creditor's debt. This right continues after the company goes into liquidation.
- 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.

A secured creditor is entitled to vote at creditors' meetings for the amount the company owes them less the amount they are likely to receive from realisation of the secured assets (i.e. their shortfall). The secured creditor can participate in any dividend to unsecured creditors for their shortfall.



Directors and liquidation

Directors cannot use their powers after a liquidator has been appointed. They have an obligation to assist the liquidator by:

- advising the liquidator of the location of company property and delivering the property in their possession to the liquidator
- providing the company's books and records
- advising the liquidator of the location of other company records
- providing a written report about the company's business, property, affairs and financial circumstances within:
 - ten business days of the appointment of the liquidator by the court, or
 - five business days of the appointment of a liquidator in a creditors' voluntary liquidation
- meeting with, or reporting to, the liquidator to help them with their inquiries, as reasonably required
- if required by the liquidator, attending a creditors' meeting to provide information about the company and its business, property, affairs and financial circumstances.

A liquidator has the power to apply to the court to conduct a public examination, under oath, of a director (or other person with information about the company).

If the company has traded while insolvent, ASIC, a liquidator or, in certain circumstances, a creditor can commence proceedings against directors personally for amounts lost by creditors.

Conclusion of liquidation

A liquidation comes to an end when the liquidator has realised and distributed all the company's available property and reported to ASIC.

The liquidator must lodge a final account of their receipts and payments, called an 'end of administration return' and lodge it with ASIC through ASIC Connect.

Alternatively, in a court liquidation, after the liquidator decides the company's affairs are fully wound up, they can:

- seek an order for release from the court
- seek an order for release and deregistration of the company by ASIC.

ASIC will deregister the company three months after the end of administration return is lodged.

*Disclaimer

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If any products are discussed, you should obtain a Product Disclosure Statement relating to the products and consider its contents before making any decisions. It is recommended to seek advice from a qualified professional relevant to your particular needs or interests. (For instance, Tax Advice from a Tax Agent, Financial Advice from a Licensed Financial Adviser and so on and so forth). Information has been sourced from Australian Securities & Investments Commission and Australian Restructuring Insolvency and Turnaround Association.





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