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Technical Insights

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Funding the ongoing operations of a company under administration

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- Recognizing the need for administrators on occasions to propose external funding for the company under administration.
- Administrators may seek directions from the court as to the reasonableness of the proposed funding agreement
- Cases where the courts have demonstrated willingness to provide directions orders as to the reasonableness of a proposed funding agreement.
- Other court orders relating to proposed funding agreement may concern confidentiality, limiting the personal liability of the administrator, and extending the time for registering security interests under the PPSA.

Introduction

On a company proceeding into administration under Part 5.3A Corporations Act, it often becomes apparent to the appointed administrator that external funding will need to be obtained for the purpose of meeting the company's ongoing operating costs.

Obtaining funds in these circumstances may provide the administrator with the opportunity to sell the company's business as a going concern, or alternatively to fully explore recovery and reconstruction options for the company.

By way of recent example, the administrators appointed to a WA uranium miner, Paladin Energy Ltd, sought to secure a $US60 million, 12-month financing facility to keep the company operating on a business-as-usual basis while they implemented recapitalization and restructuring strategies with a view to maximizing value for all stakeholders. The rescue effort proposed by the administrators necessitated a directions application to the Federal Court: see *Woods, in the matter of Paladin Energy Ltd (Administrators Appointed)* (2017) FCA 836.

The following discussion is concerned to identify issues that commonly arise in cases of this kind, court orders being sought, and the attitude of the courts when addressing those issues.

Reasonableness of the proposed funding arrangement

In the normal course of events, the administrator's funding proposal will have been put forward because the company is not in a position to provide the necessary funds from its own resources. It is therefore understandable in view of the company's proposed exposure to further debt often involving considerable sums that the administrator will seek directions from the court endorsing the reasonableness of the funding proposal.

With respect to directions, applications arising in the course of external administrations it should be noted that from 1 September 2017 the source of the court's power to make directions orders is contained in s 90-15 of Schedule 2, Corporations Act 2001. In the case of directions applications arising from administrations under Part 5.3A, Corporations Act, s 90-15 of Schedule 2 has replaced s 447D, Corporations Act.

Early indications from the courts suggest that the courts will be willing to exercise the power to make directions orders under s 90-15 in accordance with long-standing principles previously applied in sections such as s 447D: see *Walley, in the matter of Poles & Underground Pty Ltd (Administrators Appointed)* (2017) FCA 486 at para. 41.

In this respect, there are well recognised limitations in which directions are given. For example, the courts have refrained from giving directions where the directions sought would merely have the effect of substituting the court's commercial assessment of the funding proposal for the administrator's. There needs to be more, such as legal controversy as to whether the funding proposal places the

administrator in a potential conflict of interest; or where the propriety or competency of the administrator's decision making is under attack.

In this last respect, the administrator may have encountered opposition to the funding arrangement from certain creditors questioning the appropriateness of the proposal. Their objections together with the prospect of future legal proceedings give rise to concerns as to the propriety and reasonableness of the administrator's decision such as to justify an administrator's application for directions. A directions order obtained in these circumstances supporting the administrator's conclusions as to both the need for a funding proposal and the terms thereof will provide the administrator with protection against claims of unjustifiable or unreasonable decision making in proposing and implementing the funding agreement: see *Mentha, in the matter of Arrium Limited (administrators appointed)* (2016) FCA 972.

Confidentiality

Pursuant to statutory provisions existing in the various State and Commonwealth jurisdictions the courts have the power to make suppression or non-publication orders on the grounds that the order is necessary to prevent prejudice to the proper administration of justice: see, for example, s 37AG, Federal Court of Australia Act 1976 (Cth).

In the present context, administrators may seek orders to ensure that the proposed funding agreements before the court are kept confidential. The courts have demonstrated willingness to protect material of a commercially confidential and sensitive nature. There is a clear public interest in the effective administration of insolvent companies for the benefit of creditors, and this is a relevant consideration in favour of confidentiality orders. As observed by the Court in *Woods, in the matter of Paladin Ltd (Administrators Appointed)* (2017) FCA 836:

"The commercial interests of the companies should be respected, particularly at a time of considerable commercial sensitivities concerning the future operation of the activities of the companies." (para.37).

Limiting the administrator's personal liability for borrowings under the funding agreement

By procuring a funding agreement for a company under administration, the administrator incurs personal liability for repayment obligations arising under the agreement: see s 443A (1) and (2), Corporations Act. Understandably, administrators will be reluctant to accept such personal liability particularly as the funding is designed to promote the interests of the company and its creditors and not the personal interests of the administrator.

As a result, administrators have invariably sought modification of s 443A to exclude unqualified personal liability for debts arising out of the funding agreement. In this regard, it is well established that the court has power under s 447A, Corporations Act to limit the administrator's personal liability under s 443A, and that in appropriate cases such an order will be made. As observed by the Court in *Mentha, in the matter of Arrium Ltd (administrators appointed)* (2016) FCA 972:

"Most of the cases where the courts have exercised its powers under s 447A to vary the administrator's liability under s 443A have involved administrators borrowing funds during the period of the administration. The orders typically sought have the effect of limiting recourse … to the administrator personally to the extent to which he or she is able to be indemnified from the assets of the company." (para. 31).

Fixing the time under s 588FL, Corporations Act for registration of the funder's security interest under the Personal Property Securities Act (PPSA)

Where the lender under the proposed funding agreement seeks to obtain security over the company's personal property for the moneys that are advanced the potential operation of s 588FL, Corporations Act needs to be taken into account.

Section 588FL deals with the avoidance of security interests perfected by registration under the PPSA in the event that an effective registration of the security interest is not made within the time set by s 588FL. Under that section, the deadline for registration is the earlier of the time that is the end of 20 business days after the security interest came into force, and the date on which the administration began.

In the circumstances of post-administration, secured funding it is apparent that on a strict reading of s 588FL a PPSA security interest granted in favour of a lender by the company under administration will fall outside the deadline for registration having been granted after the date on which the administration began, that date being the relevant deadline for registration under the terms of s 588FL.

For this reason, the administrator will be obliged to seek an order under s 588FM, Corporations Act extending the time for the security interest to be registered under the PPSA. Obtaining an extension of the registration time to a post-administration date, e.g. within 20 business days of the security interest arising, will ensure that setting aside the security interest under s 588FL on grounds that the administration has already passed will be avoided: see *K. J. Renfrey Nominees Pty Ltd (Trustee), in the matter of OneSteel Manufacturing Pty Ltd* (2017) FCA 325.

Summary

It is not unusual for an administrator following his or her appointment to form the view that in order for the company under administration to continue operating it will be necessary to arrange external funding.

In view of the urgency which often arises in cases of this kind, and the prospect of the company incurring further debt at a time when it is under financial stress, it is understandable that administrators will be concerned at short notice to involve the court through supportive directions orders, modification of Corporations Act provisions, and extensions of time in order to give effect to the funding proposal.

The above discussion has identified typical orders being sought by administrators, the reasons for those orders being sought, and the attitude of the courts in dealing with the applications at hand. In all cases, the onus is on the administrator to lead evidence that the company's entry into the proposed funding agreement is in the best interests of all stakeholders while also being consistent with the object of Part 5.3A, Corporations Act.

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