BRI Ferrier

TECHNICAL INSIGHTS

Issue 2 - 2017

Liquidators Becoming Administrators: The Supervisory Role of the Courts

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Introduction

Following the court appointment of a liquidator to a company to be wound up in insolvency the liquidator may form the view that the interests of creditors and the company would be best served by allowing the company to avoid winding up, and to enter into a deed of company arrangement with creditors under Part 5.3A of the Corporations Act.

Where a liquidator forms this view it will be necessary first to transition the insolvent company from winding up into voluntary administration and to appoint an administrator. In this last respect it is common for the liquidator to propose that he or she be appointed administrator.

In the event that such transition occurs, a further question arises, namely, where the creditors accept a deed of company arrangement what becomes of the winding up process previously implemented and still on foot?

It is apparent that there are opportunities for the courts through the exercise of judicial discretion granted under the Corporations Act to supervise the proposed transition from winding up to a deed of company arrangement. Effectively the Corporations Act recognizes two stages where the courts have the opportunity to exercise control. The first is where the liquidator has approached the court to have himself or herself appointed administrator, as opposed to seeking creditor approval of the appointment. The second occurs when a court order is sought terminating the winding up in view of the acceptance by creditors of a deed of company arrangement.

Our discussion seeks to review the nature and scope of the supervisory role of the courts in this process and to identify the guidelines they have developed when called upon to exercise their judicial discretion.

Dealing with the application of a liquidator seeking leave to be appointed administrator

Where a liquidator forms the view that the creditors of a company being wound up in insolvency could usefully consider a proposed deed of company arrangement under Part 5.3A, Corporations Act, section 436B(2) provides that the liquidator may by writing appoint an administrator of the company. Moreover, with leave of the court (or approval of creditors) the liquidator may appoint himself or herself to the position of administrator.

Applications by liquidators seeking leave of the court have resulted in judicial guidelines that inform liquidators as to the matters they will need to put before the court when seeking appointment as

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administrator. Importantly, as well as informing liquidators those guidelines can be usefully taken into account by creditors in the event that the liquidator, as opposed to seeking leave of the court, seeks a creditors' resolution approving the appointment of liquidator as administrator.

When determining the position adopted by the courts on leave applications under section 436B(2) it is useful to contrast the approach of early cases with more recent decisions.

The decision of the NSW Supreme Court in *Re Depsun Pty Ltd* (1994) 13 ACSR 644 is representative of earlier cases. Here the Court took the view that it should not give its approval to any step of a procedure which it does not consider to be in the public interest. The particular concern of the Court was the prospect of the company through the administration process going back into the market place under the control of its directors without sufficient assurances as to its future financial prospects. In the opinion of the Court such assurances needed to be forthcoming before it would entertain approving the appointment of liquidator as administrator.

In recent cases the courts have adopted a more relaxed position by acknowledging that there should not be a heavy onus on the liquidator at this stage to satisfy the court that the administration process was in the public interest. It is now accepted by the courts that there will be an opportunity to fully consider that question after a deed of company arrangement has been approved by creditors, and an application was before the court to terminate the winding up which remained suspended but on foot throughout the administration process.

It is now widely acknowledged that the essential question on leave applications is whether the liquidator is an appropriate person to be appointed as administrator, rather than whether an administrator should be appointed at all. This approach can be observed in *Turk v Newmont* (1999) NSWSC 622 where the Court states:

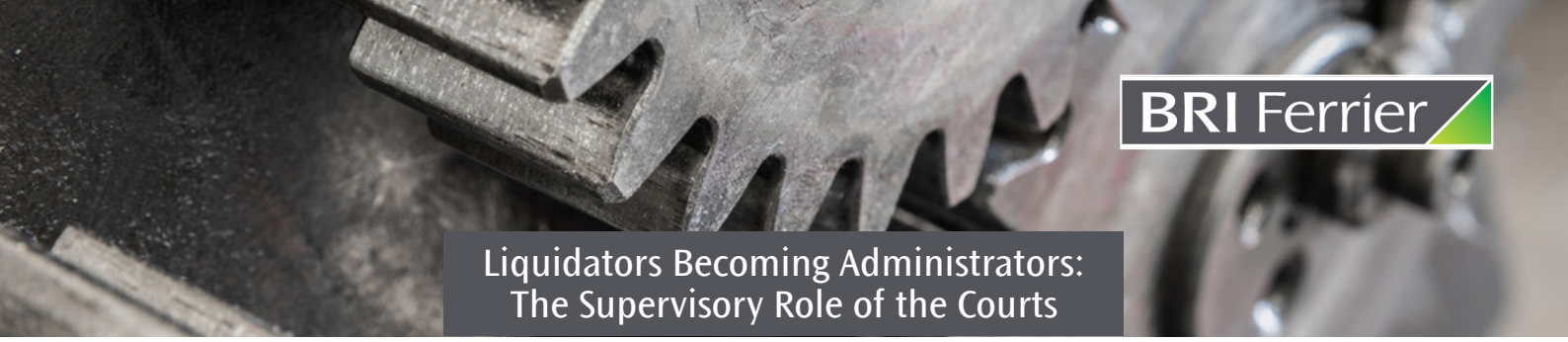
"Given that (the liquidator) has had no association with the company and its directors before being appointed liquidator by this Court and that on his evidence he has not built up any personal relationship with directors after the appointment and that he has accumulated understanding of and information about the company in the performance of his duties as liquidator, I am persuaded that he is an appropriate person for the appointment."

It may be noted that in granting leave for the liquidator's appointment as administrator the Court, in addition to the absence of conflict of interest, gave weight to the liquidator's in-depth knowledge of the company's affairs ensuring that the administration would be more cost-effective than were any other person appointed.

Termination of winding up following creditors' acceptance of a deed of company arrangement

The courts have consistently acknowledged that where a company has proceeded from liquidation into administration the liquidator's powers are suspended during the course of the administration (see section 473C, Corporations Act) but will revive when a deed of company arrangement is executed. The revival of liquidator's powers necessitates an application to the court for an order under section 482(1) terminating the winding up to enable the terms of the deed to be implemented: see *Mercy v Wanari* (2000) NSWSC 756.

It is at this stage that the court will have full details of the final deed before it and will be in a position to consider the interests of creditors, including post-deed creditors, contributories and the public interest when determining whether termination of the winding up



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is appropriate: see In the matter of *Plaza West Pty Ltd (in liquidation)(subject to deed of company arrangement)* (2013) NSWSC 168, para 14.

Importantly section 482(2A), Corporations Act directs the Court to have regard to a non-exhaustive list of factors such as any misconduct of the company's officers, the commercial substance of the creditors' decision in accepting the proposed deed of company arrangement, and whether the proposed deed would result in the company returning to solvency or not.

The objective of a deed of company arrangement to obtain for creditors a better return than they would receive in a winding up is an important factor to be taken into account by the courts when contemplating the termination of winding up. However the courts in accordance with section 482(2A)(e) recognize the significance of public interest factors at this stage, and in particular whether the likely future activities of the company presented a potential risk for future creditors in their dealings with the company.

For example, in *Vero Workers Compensation v Ferretti* (2006) NSWSC 292 the Court found that under the proposed deed of company arrangement the terms of subordination agreements relating to significant related creditor claims, coupled with a finding that the company had no assets, were considerations that outweighed the advantages to existing creditors under the deed. In the opinion of the Court the risks to future creditors were too great such that the application for termination of the winding up should be refused.

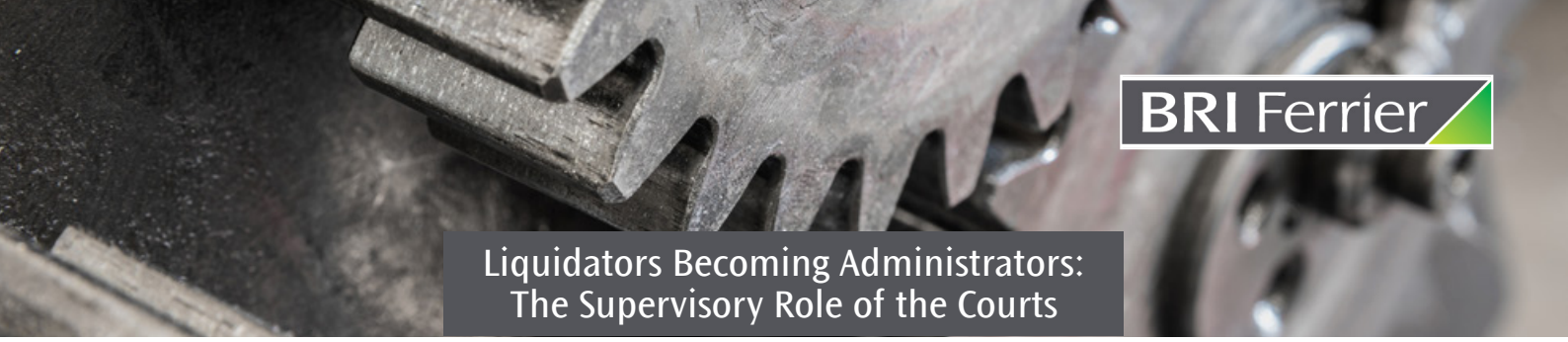
By way of contrast in In the matter of P*laza West Pty Ltd* (see above) the Court saw no reason to decline termination of the winding up. Here the Court noted that the company had taken substantial steps under the deed to restore its solvency by the capitalization of related parties' claims. This meant that the value of the company's assets significantly exceeded the amount of its debt thereby ensuring to the satisfaction of the Court that the interests of future creditors were not at risk.

Concluding comments

It is apparent that the application to the court for an order terminating winding up has proved to be an effective means of controlling a company's transition from liquidation to a deed of company arrangement.

In our discussion we have seen that a liquidator by leave of the court or approval of creditors may as administrator be given the opportunity to confer with creditors and to arrive at an arrangement designed for their benefit. However, as directed by section 482(2A), Corporations Act a court will ultimately have the opportunity to review the efforts of the administrator, the conduct of the company's officers and the terms of any proposed deed of company arrangement.

Only when the court is satisfied that under the terms of the deed the best interest of creditors has actually been achieved, and, in addition, public interest considerations addressed such as the company's financial prospects and the conduct of its officers, will the court entertain termination of the winding up and implementation of the proposed deed of company arrangement.



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