Melsom Robson
Chartered Accountants
incorporating
F I T Solutions

Voluntary Administration in a Nutshell

The regime of Voluntary Administration provides immediate protection for corporate assets and limits directors' exposure to personal liability for insolvent trading.

The regime was created in 1993 by changes to the (then) Corporations Law, to provide a viable alternative to Liquidation where companies which were viable or had viable businesses became insolvent. It provides an opportunity for insolvent companies to trade out of their difficulties in conjunction and in cooperation with, their creditors.

Voluntary Administration provides for a moratorium on debts while the Administrators, together with management, review the company's position and determine the most appropriate strategies for its future. It is, in effect, a timeout, providing management with breathing space while allowing it time to determine the most appropriate way of dealing with the company's financial predicament.

It is important to remember that the Voluntary Administration is only a moratorium, it is not an end result in itself. When a strategy, or number of strategies have been determined, a proposal is then put to creditors, who accept, modify or reject the proposal. Creditors have the ultimate say in the company's future.

The Effects of Voluntary Administration

All documentation which includes the company name must also include, immediately after the name, the words "Administrator/s Appointed".

Control of the company is in the hands of the Administrators and the directors surrender their powers as directors. If the company progresses to a DOCA, however, those powers can be restored, and often are.

Given its aims of preserving a business in the event of a trade out, Voluntary Administration contains an extremely powerful tool that is not available in any other form of external administration:-

- In a Voluntary Administration, owners of property used by the company cannot recover that property without the permission of the Administrators or an order of the Court. However, should the Administrators decide to use that property, they are liable to pay for the use of that property.

- Similarly, creditors who have director guarantees are not permitted to call up those guarantees.

In addition, all legal recovery action against the company ceases upon appointment of the Administrators, unless the court decides that they may continue. This is consistent with the concept of the moratorium.

Should the Administrators continue to trade on the company's business, the Administrators may be personally liable for any debts incurred in the course of the continuation of business. Of course, the Administrators have some form of protection in that they have a lien over the company's assets to secure those liabilities. The lien is of limited value, however, if the company has minimal assets or its assets are subject to a secured debt.

Creditors who supply goods and services to the company with the authority of the Administrators are in a privileged position of priority, ranking ahead of all other claims against the company. In addition, if the assets of the company are insufficient to cover their claims, they may claim against the Administrators personally.

The Process Itself

The first step in the process is for directors, at a properly convened meeting, resolving to place the company into Voluntary Administration, and to appoint the Administrators.

The Administrators then take immediate steps to locate and protect the company's assets. They will also work with the directors to determine the feasibility and mode of continued trading. Given the personal liability aspect, certain control measures will be instituted, especially in regard to incurring credit.

The Administrators will also conduct preliminary investigation into the company's affairs and consider the likelihood of recovery of voidable transactions in the event of liquidation.

First Meeting of Creditors

- The Administrators must convene a meeting of creditors to be held within eight (8) business days of their appointment with at least five (5) business days notice.
- At this first meeting, the only matters for resolution by the creditors are whether to appoint other Administrators and whether to appoint a Committee of Creditors.
- A Committee of Creditors may be useful to provide advice to the Administrators and to act as a conduit to other creditors. It has no powers to vote and cannot force the Administrators to undertake, or refrain from any course of action.

After the first meeting, the Administrators will prepare a report to creditors. This report will cover, inter alia, background information on the company and its directors, results (as can be made public) of their investigations, an analysis of the company's financial position and, if a Deed of Company Arrangement has been proposed, a copy of the proposal, a summary of its terms and the Administrators' views on the Deed.

In providing that view, the Administrators ought to compare the outcome, for creditors, of the Deed as opposed to any other alternative.

Second meeting of creditors
The Administrators are required to convene a second meeting of creditors within five (5) business days (before or after) the end of the convening period. Unless extended by the Court, the convening period itself is twenty (20) business days beginning on the next business day after the administration begins (or twenty-five (25) business days if appointed in December or within 25 business days before Good Friday) to determine the fate of the company. At this second meeting, creditors have three options to vote on:

- If a proposal is submitted and accepted by creditors, the company then progresses to a Deed of Company Arrangement ("DOCA"). It should be noted that when the company reaches this stage, it is no longer in Voluntary Administration, but is "subject to a Deed of Company Arrangement". These words must be included immediately after the company's name.
- If directors cannot or do not come up with an acceptable proposal, or believe that the company, or business, is not viable in the long term, liquidation is the most likely outcome. The words "In Liquidation" must be used after the company name.
- If on the other hand, investigation or subsequent events show that the company is viable and that formal administration is unnecessary, or inappropriate, creditors may decide to release the company from Administration in which case it reverts to its former status.

- In considering a proposal for a Deed of Company Arrangement, creditors consider the possible returns from the deed as compared to liquidation.
- For a resolution to be passed, a majority in number and value of those present and voting is required.
- All creditors, with the possible exception of secured creditors, are bound by the decision of the meeting

Should the creditors not be in a position to resolve to determine the company's fate, they may resolve to adjourn the second meeting for a period of up to forty-five (45) businessdays. This may be further extended by application to the court, provided the application is made before the expiry date.

Deed of Company Arrangement
If creditors resolve in favour of a Deed of Company Arrangement, a Deed is prepared by a solicitor and must be executed by the company within fifteen (15) business days of the date of the meeting. Failure to do so, will result in the company being immediately placed into liquidation, with the Administrators becoming the liquidators.

The company's status changes from "Administrators Appointed" to "Subject to Deed of Company Arrangement" only after execution of the Deed by all parties to the Deed.

A Deed of Company Arrangement can be in any form - it could encompass some form of trade out, either paying creditors in full or in part, trading on while seeking external funding, a buyout, an orderly realisation of assets, or some other combination.

It may exclude certain creditors from the Deed or may alter priorities, however, it should be noted that any creditors who are adversely affected by the deed may apply to the court for the deed to be set aside.

- The most common form of exclusion is for directors and their related entities choosing not to compete with other creditors for available funds.

- The most common form of alteration to priorities is to allow small creditors to be paid in full. This often has minimal effect on other creditors and reduces the cost of preparing dividend cheques, especially where minor dividends are being paid.

The Deed could (and normally does) return the power to run the company to the directors. In that case, the Deed Administrators may have a monitoring role, to ensure that creditors' interests are being protected.

The administrator of the Deed is known as the Deed Administrator.

Once the company is subject to a Deed of Company Arrangement, the moratorium against owners of property and guaranteed creditors ceases, unless the Deed provides for their continuation. The moratorium against legal actions and unsecured creditors who are bound by the deed continues, unless specifically excluded.

Secured Creditors
On the appointment of Administrators, Secured Creditors have only thirteen (13) business days ("decision period") from initial notification to decide whether to appoint Receivers over the company's assets.

If Receivers are appointed, they take control of the company and the Administrators adopt a back seat role with regard to the assets and the ongoing business, although the Administrators are still required to conduct investigations and to call meetings, etc.

If the secured creditors do not appoint Receivers within the decision period, they are bound by the moratorium that applies to all creditors.

At the second meeting, all creditors are bound by the decision unless, as secured creditors, they either abstain or vote against the resolution.

Termination
When a Deed has been successfully completed and its terms met, the company then reverts to its former status with all debts covered by the deed being discharged.

However, should the Deed be incapable of performance in its current form, it may be terminated or varied by the creditors.

Should creditors decide to terminate the Deed, they may also resolve that the company then proceed into liquidation.

George Lopez