

Global Economic Downturn fact sheet

Insolvency – Voluntary administration

Series 1 – Issue 10

As part of the Institute's ongoing efforts to provide members with guidance and information on key issues affecting the current business environment, the Institute have developed a practical factsheet series, which presents guidance for members written by members.

'It is the directors' duty to exercise powers and duties in good faith and in the best interests of the company.'

The facts on voluntary administration

Michael Jones BA FCA, Jones Partners Insolvency and Business Recovery, Chartered Accountants

This factsheet provides guidance on identifying when a company may be insolvent and the facts on voluntary administration as an option to directors in these circumstances.

Indicators of insolvency

The courts have summarised the indicators of insolvency as follows:

1. Continuing losses
2. Liquidity ratios below 1
3. Overdue Commonwealth and state taxes
4. Poor relationship with present bank, including inability to borrow further funds
5. No access to alternative finance
6. Inability to raise further equity capital
7. Suppliers placing (company) on COD, or otherwise demanding special payments before resuming supply
8. Creditors unpaid outside trading terms
9. Issuing of post-dated cheques
10. Dishonoured cheques
11. Special arrangements with selected creditors
12. Solicitor's letters, summons(es), judgements or warrants issued against the company
13. Payments to creditors or rounded sums which are not reconcilable to specific invoices
14. Inability to produce timely and accurate financial information to display the company's trading performances and financial position, and make reliable forecasts.

Directors' duties

1. To prevent insolvent trading, not incur a debt if the company is insolvent at the time
2. To keep books and records that correctly record and explain its transactions and financial position and performance and would enable true and fair financial statements to be prepared and audited
3. To exercise powers and duties with the care and diligence that a reasonable person would have
4. To exercise powers and duties in good faith in the best interests of the company and for a proper purpose
5. Not improperly use position to gain personal advantage, or to cause detriment to the company
6. Not improperly use information to gain personal advantage, or to cause detriment to the company.

Voluntary administration

A voluntary administration provides a company with a viable opportunity to put a proposal to creditors and avoid winding up. The main purpose is to preserve the company structure, its business or to simply provide a better result for the creditors than winding up.

Continued overleaf >

The main benefits of a voluntary administration are:

1. Freeze the company's creditors giving the company breathing space to assess its future and financial position
2. Maximise the return of the company's assets enabling the sale of the business as a going concern
3. Enables the company to continue to trade while its future is being evaluated
4. Creditors receive a report from an administrator (who is independent of the directors). This report deals with company's financial position, its future and the options available to creditors
5. Enables the creditors to consider a proposal and collectively vote on its acceptance or otherwise.

The procedures

1. An administrator is appointed by the director or secured creditor or liquidator
2. The administrator must convene a meeting of creditors (the first meeting) within eight business days after the appointment to enable creditors to appoint a different administrator and/or form a committee of creditors
3. The administrator investigates the company's affairs and reports to creditors on:
 - > The company's background
 - > The company's financial position
 - > The reasons for its difficulties
 - > The conduct of directors and potential offences
 - > Legal action available to the company or a future liquidator
 - > Details of any proposal for creditors' consideration
 - > The alternatives available to the company and creditors
 - > The likely return to creditors pursuant to the aforementioned alternatives.
4. The administrator must convene a further meeting (the decision meeting) within 20 business days of the appointment, (25 days if at Christmas or Easter)
5. At this meeting the creditors must vote:
 - > To wind up the company
 - > To accept the proposed Deed of Company Arrangement (D.O.C.A.)
 - > To adjourn the meeting for further consideration
 - > To end the administration.

6. The meeting may be adjourned for a further 45 business days or longer with leave of the court.

If the deed is accepted

1. A document is prepared, executed and signed setting out the precise details or terms of the arrangement
2. The deed may be terminated or varied at a later time by resolution of creditors
3. When the deed is executed, the administration comes to an end and the company is no longer under the control of the administrator
4. The administrator of the company (usually, but not necessarily) becomes the administrator of the *Deed of Company Arrangement* (the deed administrator)
5. The deed administrator must ensure that its terms are carried out
6. If the terms are not carried out in accordance with the deed, the deed administrator would convene a meeting of creditors to either amend or terminate the deed
7. If the deed is terminated, the company is usually wound up.

If the deed is not accepted

1. The creditors may end the administration leaving the company exposed to the same legal action as before the administration commenced
2. The creditors may further adjourn to consider amendments to the proposal
3. The creditors may wind up the company – usually (but not necessarily) appoint the administrator to be the liquidator.

Further information

Further information of a voluntary administration and *Deeds of Company Arrangements* can be obtained from the ASIC and Insolvency Practitioners websites. For links to these websites and more information, guidance and tools on the global economic downturn refer to [charteredaccountants.com.au/news_issues/global_economic_downturn](https://www.charteredaccountants.com.au/news_issues/global_economic_downturn).

It is important to note, the above fact sheet is designed to be general in nature and each case needs to be dealt with on its individual merits. The Institute maintains a list of specialist insolvency practitioners who may be consulted on these matters, <https://members.charteredaccountants.com.au/Customer/Custom/FindCA/CASearch.asp>

About the author

Michael G Jones FCA is an Official Liquidator appointed by the Supreme Court of New South Wales and a Registered Trustee in Bankruptcy. Michael was also a former State Councillor of the Institute of Chartered Accountants in Australia and served on a number of Committees.

Michael has over 30 years of experience in the profession and has been involved in many large corporate insolvency matters, including many turnarounds.

For further enquiries please contact Michael Jones FCA on:

Email mjones@jonespartners.net.au **Phone** 02 9251 5222

Web www.jonespartners.net.au **Fax** 02 9251 5222



Neither the Institute nor any of its directors, staff and associates shall be liable on any ground whatsoever to any party in respect of decisions or actions they may take as a result of using this publication nor in respect of any errors in, or omissions from it. The information contained in this publication is a general commentary only and should not be used, relied upon or treated as a substitute for specific professional advice. This publication presents the views and opinions of the author and not necessarily those of the Institute.