Receivership: A guide for creditors

Information sheet – 54

This is **Information Sheet 54 (INFO 54)**. It provides information for unsecured creditors of companies in receivership.

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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. Lenders might require a security interest in company assets when they provide a loan. If the creditor wants to ensure their security interest over personal property other than land is enforceable and given priority in an insolvency, they should register the security on the Personal Property Securities Register (PPSR) You can search the PPSR to find out if anyone holds a security interest (other than a mortgage over land) in the company's assets.
- An **unsecured creditor** does not hold a security interest in the company's assets.

Employees are a special category of unsecured creditor. In a receivership, in certain circumstances, some outstanding employee entitlements are paid

before the debt of the secured creditor is repaid. For more information, see Information Sheet 55 *Receivership: A guide for employees* (INFO 55).

All references in this information sheet to 'creditors' are to unsecured creditors unless otherwise stated.

The purpose of receivership

The secured creditor – via the receiver – takes control and usually protects, collects and sells some or all the company's assets. This is done for the company to repay debts owed to the secured creditor. A court-appointed receiver may also take control of and sell company property if the court order provides that power. Court receiverships are not covered in this information sheet.

The secured creditor can appoint a receiver because they hold a security interest that allows them to appoint a receiver. The security interest may comprise:

- a non-circulating security interest (e.g. a security interest in land, plant and equipment)
- a circulating security interest in assets that are used and disposed of in the course of normal trading operations (e.g. a security interest in debtors, cash and stock).

The powers of the receiver are set out in the security agreement and the *Corporations Act 2001*.

Sometimes the terms of appointment give the receiver the power to manage the company's affairs. In these cases, a receiver is known as a receiver and manager.

It is possible for a company in receivership to also be in provisional liquidation, liquidation, voluntary administration or subject to a deed of company arrangement.

The receiver's role

Generally, the receiver's role is to:

- collect and sell enough of the secured assets to repay the debt owed to the secured creditor (this may include selling assets or the company's business)
- pay out the money collected in the order required by law

- report to ASIC any possible offences or other irregular matters they come across.

The receiver's principal duty is to the secured creditor. The main duty owed to unsecured creditors is an obligation to take reasonable care to sell secured assets for not less than market value or, if there is no market value, the best price reasonably obtainable. A receiver also has the same general duties as a company director.

The receiver has no obligation to report to unsecured creditors about the receivership, either by calling a meeting or in writing. However, the receiver will usually write to the company's suppliers to inform them of their appointment. Unsecured creditors are not entitled to see the receiver's reports to the secured creditor.

A receiver must lodge with ASIC a detailed list of their receipts and payments (known as the annual administration return) each year on the anniversary of their appointment. A copy of these detailed lists of receipts and payments can be obtained by searching ASIC Connect for a fee.

Distribution of money

A receiver will usually obtain money from the assets they are appointed over by selling them. To sell a company's business, the receiver may continue to trade the business until they sell it as a going concern.

Once the receiver sells the assets, the money collected is distributed as follows:

- money from the sale of non-circulating assets is paid to the secured creditor after the costs and fees of the receiver in collecting this money have been paid
- money from the sale of circulating assets is paid out in the following order:
  - the receiver's costs and fees in collecting this money
  - certain priority claims, including employee entitlements (if the liability for these has not been transferred to a new owner)
  - repayment of the secured creditor's debt.

In both cases, any funds left over are paid to the company or its external administrator, if one has been appointed.

If the receiver is appointed under a security interest comprising both non-circulating and circulating security interests (which is common), there will be costs and fees of the receivership that cannot be directly allocated to

money from selling the non-circulating assets or circulating assets. These costs are allocated in proportion to the amount obtained from selling the non-circulating assets and circulating assets.

If employee entitlements are paid by the receiver under a circulating security interest, the payments are made in the following order:

- outstanding wages and superannuation
- outstanding leave of absence (e.g. annual leave and long service leave)
- retrenchment pay.

Each category (or class) 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).

The receiver has no obligation to pay any other unsecured creditors for outstanding pre-appointment debts.

Purchases of goods and services by receiver

If the receiver incurs debts for the purchase of goods and services during the receivership under the receiver's authority, these are paid from asset sales as costs of the receivership. The receiver is personally liable to pay for these costs if there are insufficient funds available from asset sales.

To have the benefit of this protection, you should ensure you receive a purchase order authorised in the manner advised by the receiver.

If the receiver continues to use, occupy or hold property owned by another party that is in the company's possession or occupied by the company, they are personally liable for any rent or amounts payable arising after seven days from the beginning of the receivership. The receiver can avoid this liability by informing the other party within seven days from their appointment that they do not intend to use the property.

Pre-existing contracts

The appointment of a receiver does not automatically terminate pre-receivership contracts with the company. The contract may remain current without the receiver having personal liability for the company's obligations under the contract. If you have such a contract, you may wish to seek legal advice because the law in this area is complex.

Receiver's fees

The receiver is entitled to be paid their fees from the sale of secured assets. How the fees are calculated is usually set out in the security agreement and appointment document. Unsecured creditors have no role in setting or approving the receiver's fees.

ASIC, a liquidator, voluntary administrator or deed administrator of the company may apply to the court for the receiver's remuneration to be reviewed.

Other implications for unsecured creditors

Legal action may be commenced or continued against the company despite the appointment of a receiver. This means an unsecured creditor can apply to the court to have the company put into liquidation if there is an unpaid debt. You may wish to do this – particularly if the company owes you a large amount – if there are:

- expectations there will be money or property left over after realisation of the security asset and payments to/by the receiver
- possible recoveries that may be available to a liquidator for the benefit of unsecured creditors, which are not available to a receiver
- potential offences committed by those associated with the company that a liquidator can investigate
- reasons for the liquidator to review the validity of the appointment of the receiver and the security interest, and to monitor the progress of the receivership.

Surplus property

If there are any assets or money left over when the receivership is complete, they will be returned to the company (and the control of the company's directors) unless a liquidator or another external administrator is appointed.

If a liquidator is appointed, they must carry out the liquidation for the benefit of all unsecured creditors. For more information, see Information Sheet 45 *Liquidation: A guide for creditors* (INFO 45).

Recoveries available to a liquidator

Recoveries available to a liquidator for the benefit of unsecured creditors that are not available to a receiver include:

- unfair preference payments (payments 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 phoenix activity.

Investigation by liquidator

Although a receiver must report to ASIC on any possible offences or irregularities, they do not have a specific duty to investigate and report on the affairs of the company.

A liquidator will usually carry out a more detailed investigation on behalf of all unsecured creditors to determine:

- reasons for the failure of the company
- what assets may be recoverable for the benefit of unsecured creditors
- possible offences.

The liquidator must lodge a report with ASIC if they believe offences may have been committed or the company may be unable to pay ordinary unsecured creditors a dividend (repayment of their debts) of more than 50 cents in the dollar. ASIC may act based on these reports, including banning a director if that person has been a director of two or more companies that have gone into liquidation. Similar grounds for banning a person as a director do not apply to directors of companies that have only gone into receivership.

Review of receivership

If a liquidator is appointed over a company in receivership, they will review the validity of the security interest and the appointment of the receiver.

A liquidator is usually better placed than individual unsecured creditors to monitor the progress of the receivership and report back to all unsecured creditors.

Directors and receivership

Receivership does not affect the legal existence of the company. The directors continue to hold office, but their powers depend on the powers of the receiver and the extent of the assets over which the receiver is appointed.

Control of the secured assets, which often includes the company's business, is taken away from the directors.

Directors must provide the receiver with a Report on Company Activities and Property and allow the receiver access to books and records about the secured assets.

Conclusion of receivership

A receivership usually ends when the receiver has:

- collected and sold all or enough secured assets to repay the secured creditor
- completed all their receivership duties
- paid their receivership liabilities.

Generally, the receiver resigns or is discharged by the secured creditor. Unless another external administrator has been appointed, full control of the company and any remaining assets goes back to the directors.

Questions and complaints

Contact the receiver to raise any questions or complaints. If this fails to resolve your concerns, including any concerns about the receiver's conduct, you can lodge a report of misconduct with ASIC. Reports of misconduct against companies and their officers can also be made to ASIC. ASIC does not usually become involved in matters of commercial judgement by a receiver.

More information

- Information Sheet 39 *Insolvency information for directors, employees, creditors and shareholders* (INFO 39).
- Australian Restructuring Insolvency & Turnaround Association (ARITA) website
- ARITA Code of Professional Practice for Insolvency Practitioners

Important notice

Please note that this information sheet is a summary giving you basic information about a particular topic. It does not cover the whole of the relevant law regarding that topic, and it is not a substitute for professional advice. We encourage you to

seek your own professional advice to find out how the applicable laws apply to you, as it is your responsibility to determine your obligations.

You should also note that because this information sheet avoids legal language wherever possible, it might include some generalisations about the application of the law. Some provisions of the law referred to have exceptions or important qualifications. In most cases, your particular circumstances must be taken into account when determining how the law applies to you.

> Information sheets provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.
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