Independence of external administrators: A guide for creditors

Information sheet – 84

> This is **Information Sheet 84 (INFO 84)**. It provides general information for unsecured creditors in a liquidation, voluntary administration or deed of company arrangement (DOCA) to help you decide whether the external administrator is independent.

The independence requirement in a receivership or a scheme of arrangement is not covered in this information sheet.

If a company is insolvent or in financial difficulty, it can be put into external administration. The most common forms of external administration are:

- liquidation
- voluntary administration (which may lead to a DOCA).

A company can also have a receiver, or receiver and manager, appointed, usually by a secured creditor that holds a security interest in some or all the company's property.

When a company enters liquidation, voluntary administration or a DOCA, the person put in charge (the 'external administrator' who is a registered liquidator) must be independent of the company and its directors. This is important because the external administrator must act in the interests of all creditors.

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What it means to be independent

There are different groups of people with different interests involved in the insolvency of a company. These include directors, shareholders, creditors who hold a security interest in the company's assets, unsecured creditors, employees (who may also be creditors) and customers. The external administrator must treat all groups fairly and in accordance with their legal rights. For an external administrator to be independent, they must:

- not be biased towards any person or group
- not have, or have had, a close personal or business relationship with any person involved in the insolvency where that relationship might lead a fair-minded observer to reasonably believe the external administrator might not bring an impartial mind to their work
- not be in a position where their own personal or private interests conflict with their duties in the external administration.

It is important the external administrator is independent and seen to be independent by people interested in the company's affairs. An external administrator may not be seen as being independent if there is a chance circumstances exist that might threaten the person's independence in the future.

Who may be appointed?

Only a registered liquidator can be appointed as an external administrator of a company.

If the person knows at the time they agree to accept the appointment that there is a prospect of a threat to actual or perceived independence arising in the future, the person should not accept the appointment without the court's approval (even if they tell creditors about the threat).

Relationships that prevent appointment

A person must not be appointed as an external administrator of an insolvent company if they have certain relationships with the company, unless the court gives its approval. These relationships are

- either the person or a company where the person is a substantial shareholder owes more than $5,000 to the company or a related company
- the person is owed more than $5,000 by the company or a related company (other than fees owed through their role as an external administrator)
- the person is a director, secretary, senior manager or employee of the company
- the person is a director, secretary, senior manager or employee of a company that is a secured creditor of the property of the company
- the person is an auditor of the company
- the person is a partner or employee of an auditor of the company

- the person is a partner, employer or employee of an officer of the company
- the person is a partner or employee of an employee of an officer of the company.

The person must also consider other relationships they may have had with the company or its directors, such as work done before the appointment and advice provided when deciding whether they are independent or will be seen to be independent.

Disclosing relationships

Before a liquidator is appointed by the court, they should tell the court of any circumstances they are aware of that might cause doubts about their independence.

A person who consents to act as a voluntary administrator must send to creditors a declaration about any relationships they may have. This declaration is sent with the notice of the first meeting of creditors. A liquidator in a creditors' voluntary liquidation must send to creditors within 10 business days after their appointment, a declaration about any relationships they have.

The declaration must:

- set out whether the person, their partners in a firm, or their company or an associated company has, or has had in the past two years, a relationship with either:
  - the insolvent company
  - an associate of that company
  - a former liquidator or former provisional liquidator of that company
  - a secured creditor who holds a security interest in the whole or substantially the whole of the company's property
- state the person's reasons for believing that none of the relationships result in the person having a conflict in accepting the appointment.

The declaration must also be tabled at the meeting of creditors and lodged with ASIC.

If the voluntary administrator or liquidator later realises that the original declaration is out of date or contains an error, they must as soon as practicable, prepare a replacement declaration. The voluntary administrator or liquidator must table the replacement declaration at the next meeting of creditors (or the next meeting of the committee of

inspection if a committee has been formed and its next meeting occurs before the next meeting of creditors).

A person who consents to act as an external administrator must also explain in writing details of any indemnities they receive or will receive to cover, for example, their fees and costs.

The declaration should allow you to consider the person's independence and help you decide whether you want to replace the person with another registered liquidator of your choice.

If you receive a declaration of relationships or indemnities – and are concerned the circumstances described in it might cast doubt on whether the registered liquidator is independent – you should ask them for further information. You might then consider whether they should be replaced.

Replacing an external administrator

Before a registered liquidator accepts an appointment as an external administrator, they must make reasonable inquiries to check there are no real or perceived threats to their independence.

The person must continue to monitor their independence during their appointment and take appropriate action should a threat to their independence arise. Depending on the threat, this may involve applying to the court or calling a meeting of creditors to give details of the potential threat. The court or creditors can then decide if and how the threat can be managed or whether to replace the person.

In some circumstances, creditors may seek to remove and replace the person if there are doubts about their independence. Any replacement external administrator must also prepare the relevant declarations about their relationships with various specified parties and any indemnities they may or will receive for their fees and costs.

Liquidation

Creditors in either a creditors' voluntary liquidation or court liquidation can, by resolution passed at a meeting, remove the liquidator and appoint another person as the liquidator. Creditors must be given at least five business days' notice of the meeting. A copy of the proposed replacement external administrator's declaration of relevant relationships must be given to creditors with the notice of meeting. For more information about creditors' rights to remove and replace the liquidator, see Information Sheet 45 *Liquidation: A guide for creditors* (INFO 45).

Voluntary administration

In a voluntary administration you can replace an administrator at the first meeting of creditors if another administrator has consented to act as the external administrator. A majority of creditors (in number and value) must approve the appointment of the replacement administrator. If you are a creditor, see Information Sheet 74 *Voluntary administration: A guide for creditors* (INFO 74).

If, at the second meeting of creditors in a voluntary administration, creditors vote that the company be placed into liquidation, the voluntary administrator usually becomes the liquidator of the company. Creditors may vote, by majority in number and value, to appoint another person to act as liquidator.

Deed of company arrangement

At the second creditors' meeting in the voluntary administration where creditors agree to accept the proposal for a DOCA, they can also choose the deed administrator. This person does not have to be the current voluntary administrator but may be someone else that creditors choose.

If the DOCA fails and creditors resolve to terminate the deed and wind up the company, they can also choose someone other than the deed administrator to be the liquidator (provided the other person has agreed to act as liquidator in writing).

Questions and complaints

Contact the external administrator to raise questions or complaints. If this fails to resolve your concerns, including any concerns about their conduct, you can lodge a report of misconduct with ASIC. ASIC does not usually become involved in matters of an external administrator's commercial judgement.

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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