ASIC
Australian Securities & Investments Commission

Liquidation: a guide for creditors

If a company is in financial difficulty, its shareholders, creditors or the court can put the company into liquidation.

This information sheet provides general information for unsecured creditors of companies in liquidation.

Who is a creditor?

You are a creditor of a company if the company owes you money. Usually, a creditor is owed money because they have provided goods or services, or made loans to the company. An employee owed money for unpaid wages and other entitlements is also a creditor.

A person who may be owed money by the company if a certain event occurs (e.g. if they succeed in a legal claim against the company) is also a creditor, and is sometimes referred to as a 'contingent' creditor.

There are generally two categories of creditor: secured and unsecured.

A secured creditor is someone who has a 'charge', such as a mortgage, over some or all of the company's assets, to secure a debt owed by the company. Lenders usually require a charge over company assets when they provide a loan.

An unsecured creditor is a creditor who does not have a charge over the company's assets.

Employees are a special class of unsecured creditors. In a liquidation, some of their outstanding entitlements are paid in priority to the claims of other unsecured creditors. If you are an employee, see our related information sheet 'Liquidation: a guide for employees'.

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

The purpose of liquidation

The purpose of liquidation of an insolvent company is to have an independent and suitably qualified person (the liquidator) take control of the company so that its affairs can be wound up in an orderly and fair way for the benefit of all creditors.

There are two types of insolvent liquidation: creditors' voluntary and court. The most common type is a creditors' voluntary liquidation, which usually begins in one of two ways:

1. when creditors vote for liquidation following a voluntary administration or a terminated deed of company arrangement, or

2. when an insolvent company's shareholders resolve to liquidate the company, nominate a liquidator, and call a meeting of creditors to confirm that liquidator's appointment or appoint another liquidator of the creditors' choice.

In a court liquidation, a liquidator is appointed by the court to wind up a company, following an application, usually by a creditor. Others, including a director, a shareholder and ASIC, can also make a winding-up application.

After a company goes into liquidation, unsecured creditors can no longer commence or continue legal action against the company, unless the court permits.

It is possible for a company in liquidation to also be in receivership.

The liquidator's role

When a company is being liquidated because it is insolvent, the liquidator has a duty to all the company's creditors. The liquidator's role is to:

- collect, protect and realise the company's assets
- investigate and report to creditors about the company's affairs, including any unfair preferences which may be recoverable, any uncommercial transactions which may be set aside, and any possible claims against the company's officers
- enquire into the failure of the company and possible offences by people involved with the company and report to ASIC
- after payment of the costs of the liquidation, distribute the proceeds of realisation—first to priority creditors, including employees, and then to unsecured creditors, and
- apply for deregistration of the company on completion of the liquidation.

Except for lodging documents and reports required under the *Corporations Act 2001* (Corporations Act), a liquidator is not required to do any work unless there are enough assets to pay their costs.

If the company is without sufficient assets, one or more creditors may agree to reimburse a liquidator's costs and expenses of taking action to recover further assets for the benefit of creditors.

In this case, if additional assets are recovered, the liquidator or particular creditor can apply to the court for the creditor to be compensated for the risk involved in funding the liquidator's recovery action.

Recoveries from creditors

A liquidator has the ability to recover, for the benefit of all creditors, certain payments (known as unfair preferences) made by the company to individual creditors in the 6 months before the start of the liquidation.

Broadly, a creditor receives an unfair preference if, during the 6 months prior to liquidation, the company is insolvent, the creditor suspects the company is insolvent, and receives payment of their debt (or part of it) ahead of other creditors. To be an unfair preference, the payment must put the creditor receiving it in a more favourable position than other unsecured creditors.

Not all payments from the company to a creditor in the 6 months before liquidation are unfair preferences. The Corporations Act provides various defences to an unfair preference claim.

If a liquidator seeks to recover a payment that has been made to you, you may wish

to obtain independent legal advice on the merits of the liquidator's claim before repaying any money.

Creditors' meetings

A liquidator may call a creditors' meeting from time to time to inform creditors of the progress of the liquidation, to find out their wishes on a particular matter or seek approval of the liquidator's fees.

You may also use a creditors' meeting to ask questions about the liquidation and inform the liquidator about your knowledge of the company's affairs.

In a court liquidation, the liquidator is not required to call a creditors' meeting unless a matter requires creditor approval.

The only exception is that if the creditors pass a resolution requiring a creditors' meeting to be called, or at least one-tenth in value of all the creditors request the liquidator in writing to do so, the liquidator must call a creditors' meeting. However, it is unusual for this to happen, as those who make the request or pass the resolution must pay the costs of calling and holding the meeting.

In a creditors' voluntary liquidation, a meeting of the creditors must be held annually and a joint meeting of the creditors and members must be held at the end of the winding up. Creditors can require the liquidator to call a creditors' meeting at other times, the same as in a court liquidation, as long as they pay the associated costs.

The chairperson of a creditors' meeting (usually the liquidator or one of their senior staff) must prepare minutes of the meeting and a record of those who were present at the meeting and lodge them with ASIC within one month. A copy may be obtained from any ASIC Business Centre on payment of the relevant fee.

Voting at a creditors' meeting

To vote at a creditors' meeting you must lodge details of your debt or claim with the liquidator. Often, the liquidator will provide you with a form called a 'proof of debt' to be completed and returned before the meeting. Proofs of debt are discussed further below.

The chairperson of the meeting decides whether or not to accept the debt or claim for voting purposes. The chairperson may decide that a creditor does not have a valid claim or the amount of the debt cannot be determined with any certainty at the date of the meeting. In this case, they may not allow the creditor to vote at all, or only to vote for a debt of $1. This decision is only for voting purposes. It is not relevant to whether a creditor will receive a dividend.

An appeal against a decision by the chairperson to accept or reject a proof of debt or claim for voting purposes may be made to the court within 14 days after the decision.

Voting by proxy

You may appoint a proxy to attend and vote at a meeting on your behalf. A proxy can be any person who is at least 18 years old. Creditors who are companies will have to nominate a person as proxy so that they can participate in the meeting. This is done using a form sent out with the notice of meeting. The completed proxy form must be provided to the liquidator before the meeting. You can fax the proxy form to the liquidator, but must lodge the original within 72 hours of sending the faxed copy.

You can specify on the proxy form how the proxy is to vote on a particular resolution and the proxy must vote in accordance with that instruction. This is called a 'special proxy'. Alternatively, you can leave it to the proxy to decide how to vote on each of the resolutions put before

the meeting. This is called a 'general proxy'.

You can appoint the chairperson to represent you either through a special or general proxy, but they can't use the proxy to vote in favour of a resolution approving payment of the liquidator's remuneration.

Manner of voting

A vote on any resolution put to a creditors' meeting may be taken by creditors stating aloud their agreement or disagreement, or by a show of hands. Sometimes a more formal voting procedure called a 'poll' is taken.

If voting is by show of hands or by verbally signalling agreement, the resolution is passed if a majority of those present indicate agreement. It is up to the chairperson to decide if this majority has been reached.

After the vote, the chairperson must tell those present whether the resolution has been passed or lost.

The chairperson may decide to conduct a poll, or a poll can be demanded by at least two people present who are entitled to vote, or someone who holds more than 10% of the votes of those entitled to vote at the meeting. The chairperson will determine how this poll is taken.

If you intend to demand that a poll be taken, you must do so before, or as soon as, the chairperson has declared the result of a vote taken by show of hands or voices.

When a poll is conducted, a resolution is passed if:

- more than half the number of creditors who are voting (in person or by proxy) vote in favour of the resolution, and
- those creditors who are owed more than half of the total debt owed to creditors at the meeting vote in favour of the resolution.

This is referred to as a 'majority in number and value'. If no result is reached, the chairperson has a casting vote.

Chairperson's casting vote

When a poll is taken and there is a deadlock, the chairperson may use their casting vote either in favour of or against the resolution. The chairperson may also decide not to use their casting vote.

The chairperson should inform the meeting of the reasons why they cast the vote a particular way or why they chose not to use their casting vote.

If you are dissatisfied with how the chairperson exercised their casting vote or failed to use their casting vote, you may apply to court for a review of the chairperson's decision. The court may vary or set aside the resolution or order that the resolution is taken to have been passed.

Votes of related creditors

Directors and shareholders, their spouses and relatives and other entities controlled by them are entitled to attend and vote at creditors' meetings if they are creditors of the company.

If a resolution is passed, or defeated, based on the votes of these related creditors, and you are dissatisfied with the outcome, you may apply to court for the resolution to be set aside and/or for a fresh resolution to be voted on without related creditors being entitled to vote. Certain criteria must be met before the court will make such an order (e.g. the original result of the vote being against the interests of all or a class of creditors).

Committee of inspection

In both types of liquidation, the liquidator may ask creditors if they wish to appoint a

committee of inspection and, if so, who will represent the creditors on the committee.

A committee of inspection assists the liquidator, approves their fees and, in limited circumstances, approves the use of some of the liquidator's powers, on behalf of all the creditors.

Committee meetings can be arranged at short notice, which allows the liquidator to quickly obtain the committee's views on urgent matters. Shareholders may also be members of the committee.

At the first meeting in a creditors' voluntary liquidation, creditors can decide to appoint a committee of inspection.

Creditors in both types of liquidation can also request at any time that the liquidator call separate meetings of shareholders and creditors to decide whether a committee of inspection should be appointed and, if so, who will represent the shareholders and creditors on the committee. This doesn't usually happen as the creditor making the request must pay the costs of calling and holding these meetings.

A member of the committee of inspection must not, without permission from the court, accept a gift or benefit from the company or any other person, including another creditor, or purchase any of the company's property.

A committee of inspection acts by a majority in number of its members present at a meeting, but it can only act if a majority of its members attend.

A liquidator must consider any directions given by the committee of inspection, but is not bound to follow them.

Minutes of committee of inspection meetings must be prepared and lodged with ASIC within one month. A copy may be obtained from any ASIC Business Centre on payment of the relevant fee.

Approval of liquidator's fees

A liquidator is entitled to be paid for the work carried out on the liquidation, but only if there are assets available. The liquidator cannot be paid until the amount of fees has been approved by one of the methods set out in the Corporations Act.

In a court liquidation, the amount of fees is approved by:

- agreement with a committee of inspection (if there is one), or
- a resolution passed at a creditors' meeting, or
- the court.

The liquidator must try to get approval by each of these methods, in turn.

In a creditors' voluntary liquidation, a committee of inspection, or creditors, may approve the fees.

The court has the power to review the amount of fees approved.

If you are asked to approve fees, either as a member of a committee of inspection or in a general meeting of creditors, you should make sure that the amount claimed by the liquidator is reasonable given the amount of work involved in the liquidation, the difficulties encountered by the liquidator and the outcome for creditors. The liquidator should provide you with sufficient information before the meeting to enable you to make this assessment. This information includes:

- the total amount of fees sought to be approved and whether this total includes the applicable amount of GST
- how the fees were calculated, and

- a summary of the tasks performed and results achieved in the liquidation.

If you are in any doubt about how the fees were calculated, ask the liquidator for more information.

In a court liquidation, the liquidator must also send creditors a statement of all receipts and payments for the liquidation.

Apart from fees, the liquidator will also be entitled to reimbursement for out-of-pocket expenses that have arisen in carrying out the liquidation. This reimbursement does not require committee, creditor or court approval.

Payment of dividends

If there are funds left over after payment of the costs of the liquidation, and payments to other priority creditors, including employees, the liquidator will pay these to unsecured creditors as a dividend. Generally, the order in which funds are distributed is:

- costs and expenses of the liquidation, including liquidators' fees
- outstanding employee wages and superannuation
- outstanding employee leave of absence (including annual leave, sick leave—where applicable—and long service leave)
- employee retrenchment pay, and
- unsecured creditors.

Each category is 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.

Proving your debt

Before any dividend is paid to you for your debt or claim, you will need to give the liquidator sufficient information to prove your debt.

The liquidator will notify you if there are likely to be funds available for distribution and must call for formal proof of debt forms to be lodged. At least 14 days notice of the deadline for lodging the proof must be given.

This notice must be given to each person claiming to be a creditor whose debt or claim has not already been admitted by the liquidator. It must also be published in a daily newspaper in the states where the company carried out its business. A copy of the formal proof of debt form will be sent to you with the notice.

You should attach copies of any relevant invoices or other supporting documents to the proof of debt form, as your debt or claim may be rejected if there is insufficient evidence to support it.

If a creditor is a company, the proof of debt form must be signed by a person authorised by the company to do so.

The completed proof of debt form must be delivered or posted to the liquidator. When submitting your claim, ask the liquidator to acknowledge receipt of your claim and advise if any further information is needed.

The liquidator must notify you within 7 days if they reject your claim. If you are dissatisfied with the decision, your first step should be to promptly contact the liquidator to see if you can resolve the matter.

If you can't resolve the matter with the liquidator, you may wish to seek your own legal advice, as you have a limited time to appeal to the court. The liquidator will notify you of this time in the notice of rejection. It must be at least 14 days after you receive the notice. The court has the power to extend the time to appeal. If you

don't appeal within this time, the liquidator's decision on your claim is final.

If you have a query regarding the calculation of your claim, or the timing of the payment, discuss this with the liquidator.

Other creditor rights

As well as the various rights involving meetings and participation in dividends discussed above, the other rights of unsecured creditors include the right to:

- receive written reports to creditors about the liquidation
- inspect certain books of the liquidator
- inform the liquidator about your knowledge of matters relevant to the affairs of the company in liquidation, and
- complain to ASIC or the court about the liquidator's conduct in connection with their duties.

Written reports

The number of written reports a liquidator sends to creditors about the liquidation varies. If there are no funds at all available in the liquidation, it is possible that no written report will be sent, although many liquidators will send creditors a brief report even where there are no funds.

Liquidator's books

Liquidators must keep sufficient books to give a complete and correct record of their administration of the company's affairs. These include minutes of meetings and details of all the receipts and payments for the liquidation. These books must be available at the liquidator's office for inspection by creditors and shareholders.

Copies of minutes of meetings and 6-monthly detailed lists of receipts and payments, as well as a number of other documents, must also be lodged with ASIC. Copies may be obtained from any ASIC Business Centre on payment of the relevant fee.

Creditors are unable to access the company's books and records without court permission.

Informing the liquidator

The liquidator must report to ASIC if they suspect that anyone connected to the company may have committed an offence. If you have any information that might assist in preparing such a report, you should let the liquidator know.

These reports are not available for inspection. ASIC reviews these reports and decides whether to take further action, such as banning a person from acting as a company director for a period of time or charging the person with a criminal offence.

Applications to the court

Creditors can apply to the court if they are dissatisfied with an act, omission or decision of a liquidator. This includes if a creditor seeks:

- to challenge the liquidator's decision not to admit a proof of debt or claim, either for voting or dividend purposes, and
- a review of the liquidator's fees, in certain circumstances.

Making an application to the court can be costly. You should attempt to resolve any problems with the liquidator and only go to court if this fails.

Liquidators, ASIC and other people can also make applications to the court. For example, a liquidator might apply to have questions decided or powers exercised in a liquidation.

Complaining to ASIC about a liquidator's conduct is discussed below.

Secured creditors' rights

If a company fails to meet its obligations under a charge (e.g. mortgage), a secured creditor can appoint an independent and suitably qualified person (a receiver) to take control of and realise some or all of the charged assets, in order to repay the secured creditor's debt. This right continues after the company goes into liquidation. For more on receivership, see ASIC's 'Receivership: a guide for creditors' information sheet.

Another option available to a secured creditor of a company in liquidation is to ask the liquidator to deal with the secured assets for them and account to them for the proceeds and costs of collecting and selling those assets.

A secured creditor is entitled to vote at creditors' meetings for the amount the company owes them that exceeds the amount they are likely to receive from realisation of the charged assets. The secured creditor can participate in any dividend to unsecured creditors on a similar basis.

Directors and liquidation

Directors cannot use their powers after a liquidator has been appointed. They have an obligation to assist the liquidator by:

- advising the liquidator of the location of company property and delivering any such property in their possession to the liquidator
- providing the company's books and records to the liquidator
- advising the liquidator of the whereabouts of other company records
- providing a written report about the company's business, property and financial circumstances within 14 days of the appointment of the liquidator
- meeting with, or reporting to, the liquidator to help them with their enquiries, as reasonably required, and
- if required by the liquidator, attending a creditors' meeting to provide information about the company and its business, property, affairs and financial circumstances.

Generally, in a creditors' voluntary liquidation initiated by directors, one director and the company secretary must attend the first meeting of creditors.

A liquidator has the power to apply to the court to conduct a public examination, under oath, of a director (or other person with information about the company).

Compensation proceedings for amounts lost by creditors as a result of the company trading while insolvent can be initiated against a director personally by ASIC, a liquidator or, in certain circumstances, a creditor.

Conclusion of liquidation

A liquidation effectively comes to an end when the liquidator has realised and distributed all the company's available property and made their report to ASIC.

In a creditors' voluntary liquidation, the liquidator must hold a final joint meeting of the creditors and members to give an account of how the liquidation has been conducted and how company property has been disposed of. After the final meeting is held, the company is automatically deregistered by ASIC 3 months after a return of the holding of the meeting is lodged.

In a court liquidation, the liquidator is not required to hold a final meeting of creditors. After the liquidator decides that

the company's affairs are fully wound up they may:

- seek an order for release from the court
- seek an order for release and that ASIC deregister the company, or
- if there are insufficient assets to obtain a court order for the company's deregistration, request that ASIC deregister the company.

A company ceases to exist after it has been deregistered.

Queries and complaints

You should first raise any queries or complaints with the liquidator. If this fails to resolve your concerns, including any concerns about the liquidator's conduct, you can lodge a complaint with ASIC at www.asic.gov.au, or write to:

Manager National Assessment & Action
ASIC
GPO Box 9827
IN YOUR CAPITAL CITY

ASIC will usually not become involved in matters of commercial judgement by a liquidator. Complaints against companies and their officers can also be made to ASIC. For other enquiries, email ASIC through infoline@asic.gov.au, or call ASIC's Infoline on 1300 300 630 for the cost of a local call.

To find out more

For an explanation of terms used in this information sheet, see ASIC's 'Insolvency: a glossary of terms'.

For more on external administration, see ASIC's related information sheets at www.asic.gov.au/insolvencyinfosheets:

- Voluntary administration: a guide for creditors
- Voluntary administration: a guide for employees
- Liquidation: a guide for employees
- Receivership: a guide for creditors
- Receivership: a guide for employees
- Insolvency: a guide for shareholders
- Insolvency: a guide for directors

These are also available from the Insolvency Practitioners Association of Australia (IPAA) website at www.ipaa.com.au/bestpractice.

The IPAA website also contains the IPAA's Statements of Best Practice, which are applicable to their members.