External Administration in Times of Financial Uncertainty[1]

David Morrison[2] and Colin Anderson[3]

Abstract

The world financial crisis is in large part responsible for the current uncertain and challenging economic environment in Australia. This paper examines the likely impact of the general decline in economic outlook within Australia upon the increasing number of corporate reorganisations, rescues and insolvencies. We posit that the significant decline in economic health within the Australian economy may provide the first real test of the current *Corporations Act* insolvency provisions since they were introduced in June 1993. Specifically the paper considers the likely impact of the current financial crisis upon the operation of the Australian external administration provisions with respect to valuation matters and seeks to address some of the more likely immediate concerns for insolvency professionals. The paper concludes by taking the view that the corporate insolvency provisions contained within Chapter 5 of the *Corporations Act* are in good shape to handle more severe economic conditions.

Introduction

The current (and likely ongoing) economic environment in Australia is uncertain and challenging. At the time of writing the Australian economy is suffering from a general decline in economic outlook both in the short and medium term. The current economic climate of wildly fluctuating values and returns poses the question of how external administrators are to deal with those circumstances. Is it, for example, reasonable for them to assume that it is 'business as usual'?

One might be tempted to suggest that the best way forward is the 'business as usual' approach of the insolvency professional, but this presupposes that the existing provisions (particularly for voluntary administrators and controllers) have been fully tested and therefore work well in extreme circumstances of financial disarray. As a result of the financial downturn, corporate reorganisations, rescues and insolvencies are increasing in number and scale. This activity provides the first test of Chapter 5 in severe market conditions since its revamp *ex post* the *Corporations Act* amendments introduced in June 1993.

The Australian economy has not witnessed the extent of market upheaval for some considerable time[4] and certainly not since the last major legislative amendments *ex post* Harmer.[5] It is therefore reasonable to ask the question as to whether the current provisions will deal adequately with the state of the market and the extent that there might be a need for judicial recognition of market circumstances in uncertain and unusual times. Alternatively, one might

---

[1] Paper presented at 2009 Corporate Law Teachers Association Conference, Faculty of Law, University of Technology Sydney, February 2009

[2] T C Beirne School of Law, The University of Queensland; Visiting Professor University of Illinois College of Law, Spring 2007, United States of America

[3] School of Law, Queensland University of Technology

[4] Estimates vary – up to 70 years thus far; per Federal Treasurer Swan (Interview with Steve Price, Radio 2UE, Sydney, 23 January 2009), http://www.treasurer.gov.au/DisplayDocs.aspx?doc=transcripts/2009/010.htm&pageID=004&min=wms&Year=&DocType downloaded 23 January 2009; 80 years; *The Economist*, January 17-23 2009, page 9

[5] Australian Law Reform Commission *Report number 45: General Insolvency Inquiry*, (ALRC 45, 1988)

ask whether the provisions themselves are in need of clarification or extension to deal with market place changes.

This paper considers the likely impact of the current financial crisis upon the operation of the Australian external administration provisions with respect to valuation maters and seeks to address some of the more likely immediate concerns for administrators. As more companies are placed into some form of external administration there is the inevitable increased scrutiny of the insolvency practitioner. One of the key aspects of the insolvency practitioner's function involves evaluating options available and at the core of such evaluation lays the valuation decision.

One feature of the provisions in Chapter 5 is that the insolvency practitioner is expected to provide expertise in the area of valuation. There seems to have been increased demand upon the insolvency practitioner to value property and to provide advice to stakeholders. This paper seeks to:

- Identify those parts of Chapter 5 where an insolvency practitioner is required to make a valuation of assets of the company for the purposes of carrying out his or her functions;
- Discuss the issue of valuation in the current economic climate and explain why it may be difficult to adequately deal with the legal requirements currently in place; and
- Make suggestions that might enable the legislation to operate more efficaciously in the circumstances.

Particularly this paper seeks to outline issues around the extent that the liquidator, an administrator or a controller have the discretion to extend time limits in a market where asset values are fluctuating in an unusual way.

The liquidator

In a liquidation scenario, the liquidator's function is to collect and realise the assets of the company. The amount realised is then used to discharge the debts and liabilities of the company with remaining amounts (surplus) distributed among the members in accordance with the company's rules.[6] Stated in these simple terms the liquidator's function is one seemingly without much need for regulation. However, the legislation has changed over time to take into a broad range of interests. The consequence is that the legislation is no longer simple, is somewhat lengthy and as a result significant case law has developed. In following the (detailed) *Corporations Act*[7] provisions, the liquidator is supervised by the court and must have regard to resolutions made by creditors, contributories or a committee of inspection.[8]

For the most part, the collection and realisation of assets is a judgement made by the liquidator based upon their professional skill. Nonetheless, the liquidator's obligation to realise assets gives rise to general duties in carrying out that function. For example, initially the liquidator has

[6] *Re Partridge; Ex parte McDonald* (1961) 61 SR NSW 622

[7] In *Re Timberland; CAC v Harvey* (1979) 4 ACLR 259 at 282, Marks J stated that *" The duties and functions of a liquidator are to be understood primarily by reference to what is contained in the Companies Act, its rules and regulations."*

[8] Section 479(1) suggests that directions of the creditors or contributories override any given by the committee of inspection. It may also be noted that the liquidator is not controlled by the creditors or members. *"The creditors and shareholders in such a situation have no rights or powers, even collectively, to deal with a single asset or to direct how it shall be dealt with."* Per Stamp LJ in *Ayerst (Inspector of Taxes) v C & K (Construction) Ltd* [1975] 1 All ER 162

the duty to gather all of the property of the company.[9] There are clear obligations upon the liquidator therefore, to identify opportunities that increase the pool of funds available in the winding up.[10]

This is a sound principle in theory, indeed in an ideal world; a liquidator might spend a significant amount of time ensuring that all of the possible assets of a business have been identified. However the extent that a liquidator is motivated to follow through possible increases to the pool of assets will inevitably be weighed up against the likely value that the addition to the pool contributes. Therefore valuation of an asset is connected with the cost of identifying, collecting and realising that asset and there will be circumstances where one or more of those costs exceed the potential benefit of adding the asset to the pool. At this point the liquidator must make a professional judgement as to the best use of the available funds of the company for the liquidator's efforts.

The compounding aspect considered by this paper is that the considerations of the liquidator, again in an ideal world; assume steady and knowable asset prices.[11] In the particular case, the liquidator may be presented with the opportunity, (pursuant to s 568), to disclaim property considered onerous. Where valuation of assets is uncertain, or indeed where there are difficulties associated with the potential financial liability associated with an asset (such as possible environmental contamination), where the liquidator is unable to assess the likely benefit from holding the asset, there may be more inclination to disclaim the property. There is also the possible superadded difficulty in times of unpredictable financial circumstance that the liquidator is unable to identify whether property is "*not readily saleable*" [12] in terms of s 568.

The consequence of the uncertainty may lead the liquidator to be too conservative in dealing with property at the time of winding up, one possible consequence of which is that creditors will be relatively worse off not simply as a result in the diminution in the value of company assets but also in the overly cautious or fearful behaviour of the liquidator.

In the economic circumstances that we now witness, there are no safe assumptions that might be made about asset prices, except that they are less likely to be predicted with any certainty than at any time in recent history or experience, or at least within the experience of most [13]practicing liquidators and valuation experts. It is not an unreasonable assumption therefore that we will see more disputes around the value of assets and possibly disputes around professional judgement as to whether an asset is "worth" adding to the pool. These disputes will arise around the likely value of the asset where no auction is held or where an auction fails to attract bidding competition because in such circumstances the liquidator will be the person making the (ultimate) decision as to whether the asset ought to be added to the pool. From this we expect to see courts being asked, upon application, to make determinations of same. We may also expect to see valuation assessments being questioned as to their validity and increasingly courts being asked to determine, as a matter of fact, the value of an asset. This is going to be extraordinarily difficult because in our view, an increasing number of assets are

---

[9] Section 474(1)
[10] *Re Tavistock Ironworks Co* (1871) 24 LT 605
[11] Indeed by inference, it also assumes that the costs of identifying, collecting and realising assets are also knowable in advance
[12] Section 568(1)(c)
[13] (1989) 54 SASR 285 at 287

going to become impossible to value accurately. That is not a long bow to draw when we have witnessed the same problem on a larger scale in the capital markets with valuations of publicly traded securities.

There is (historic) judicial recognition of the difficult position of liquidators when dealing with the assets of an insolvent company.[14] The case law mostly deals with issues of pursuing (or failing to pursue) litigation.[15] There are fewer examples of allegations of failing to obtain the best "price" when realising the assets. In this sense a liquidator does not have the specific statutory duty that is imposed on a controller pursuant to s 420A. Rather the duty is more generally couched in terms of an obligation upon the director to act with due care and skill.[16] In the case of *Maelor Jones Investments (Noarlunga) v Heywood Smith*, Olsson J suggested there were three propositions that emerged from precedent:

- The court ought not to be unduly precipitate in condemning a person in the difficult position of a liquidator and, particularly, should not judge him with wisdom born of hindsight;
- A liquidator is not expected to exhibit a greater level of skill than may reasonably be expected of a competent person of his discipline; and
- It is certainly not every error of judgement that will be accounted negligence upon the liquidator.

Whilst there may be some comfort in these statements, more may be expected of liquidators today. It seems particularly important for the liquidator to seek advice in areas where they are unfamiliar with the assets and/or their value. This arises in cases where more difficult legal matters need to be resolved[17] and may also emerge when the assets (or their value) are unfamiliar.[18] The lesson for liquidators is likely to be that they will need to be thorough in researching the appropriate manner of conducting sales in this context given the state of the market.[19] Sound advice is an essential starting point. As colourfully put by Maugham J a liquidator may be liable if he or she attempts "*to navigate in these narrow seas, to him unaccustomed and unknown, without either chart or pilot; and for this temerarious conduct he must bear the responsibility.*"[20] The difficulty for the liquidator may nonetheless be finding a person who is able to be confident in giving the necessary advice for all the same reasons that the liquidator seeks counsel.

Recognition of the increasing requirements liquidators was demonstrated in a different context recently in *Hall v Poolman*[21] where Palmer J stated that:

---

[14] *Re Windsor Steam Coal Co Ltd* [1929] 1 Ch 151

[15] For example *Re George A Bond and Co Ltd* (1932) 32 SR (NSW) 301; *Re Ah Toy* (1986) 10 ACLR 630

[16] In *Re Windsor Steam Coal Co Ltd* [1929] 1 Ch 151 Lord Justice Lawrence stated at p 165 that if a liquidator *" incurs a loss by acting wrongly; although he may have acted honestly….the court would decline to hold either that he had acted reasonably or that he ought fairly be excused..*"

[17] As in *Re George A Bond and Co Ltd* (1932) 32 SR (NSW) 301; *Re Ah Toy* (1986) 10 ACLR 630

[18] As in *Re Timberland; CAC v Harvey* (1979) 4 ACLR 259; *Maelor Jones Investments (Noarlunga) v Heywood Smith* (1989) 54 SASR 285

[19] Some of the matters raised below regarding compliance with s 420A in relation to receivers is apt in relation to liquidators as well here

[20] *Re Home and Colonial Insurance Co Ltd* [1930] 1 Ch 102 at 125

[21] [2007] NSWSC 1330 (2007) 65 ACSR 123 at [395]

> A liquidator is appointed to salvage as much as possible for the benefit of creditors. If a proposed course of action – whether it be a legal proceeding or a commercial transaction – is not likely to produce a worthwhile benefit for creditors, the liquidator should not undertake it simply because it will generate enough to pay the liquidator's fees in undertaking that very transaction or litigation…

It will be interesting to see whether this decision is followed, given the fall in value in the financial marketplace. It might very well be considered to be entirely responsible to add seemingly negligible asset contributions to the pool in circumstances where there are slim pickings. Nonetheless, where costs of realisation escalate, due to factors such as increased advertising costs or simply the costs of holding assets, the liquidator might face unexpected losses on what otherwise appeared to be a transaction that was to add to the asset pool. In such circumstances the liquidator's actions may well give rise to a closer examination of the relevant conduct and accordingly give rise to allegations of negligence or breach of duty.

When realising company assets the liquidator is obligated to preserve the business assets.[22] One aspect of preservation is ensuring that assets such as goodwill are kept intact to the extent possible in the circumstances of liquidation.[23] This may require the business to be carried on for a period of time. Section 477(1)[24] of the *Corporations Act* sets out the general powers of a liquidator that include carrying on the business of the company insofar as it is necessary for the beneficial disposal of winding up of that business.[25] The clear intention of this provision is for the liquidator to run the business only for the time necessary. This involves a strong element of judgement on the liquidator's part and it is difficult to imagine, except in either truly hopeless cases that two independent liquidators assessing the same business might come to the same view. Necessarily, therefore courts must be cautious when assessing a liquidator's decisions in respect of s 477(1).

In respect of the decision to carry on a business, one key concern in the current market is the great deal of uncertainty around asset prices. With a lack of confidence apparent in the general market, the value of a business or of a business asset is very much a matter of estimation, since some estimates of the global market economy suggest that about half the value of listed companies has been removed from the market place. It is a game liquidator who might consider waiting for an increase in the value of an asset or an increased price for the sale of a going concern where the general direction of prices is downward. The need to obtain the best price for an asset[26] means that there is a temptation to sell sooner rather than to wait for an improved price in the current circumstances. Questions of whether a business should be continued and if so, how long the business should continue in a particular situation before it is placed on the market are fundamentally commercial in nature. There may be room for court intervention in clear cases of abuse by a liquidator[27] but current economic circumstances

---

[22] *Cleve v Financial Corp* (1873) [L R] 16 Eq 363
[23] *Re Timberland; CAC v Harvey* (1979) 4 ACLR 259
[24] Section 477 is contained within Part 5.4B – Winding up in insolvency or by the Court, Division 1A – Effect of winding up order and contains a range of general powers that the liquidator has upon appointment
[25] Section 477(1)(a)
[26] *Re Oriental Bank Corp* (1887) 56 LT 868 per Chitty J. That case demonstrates that the issue of valuation has been a vexed one for the courts and liquidators for a long time
[27] *Re Oriental Bank Corp* (1887) 56 LT 868 where Chitty J discussed this particular issue he suggested there was a tendency for liquidators to continue the business for too long. See also in a more modern context *Re Timberland; CAC v Harvey* (1979) 4 ACLR 259

suggest the problem will not be an issue in the short term because of the difficulty generally in making asset and business sales.

Section 477(2) provides for the specific powers of liquidators, including the power to sell or otherwise dispose of, in any manner, all or any part of the property of the company.[28] The usual scenario in a falling market will be for the liquidator to sell the assets at market price, market price being the best price in a competitive sale situation. The current crisis however is not simply a falling market but a fallen market. This means that there are no buyers for some business assets - whether those assets are sold independently or whether the assets are collectively sold as a business on a going concern basis. The consequence is that it might be impossible to ensure a competitive bidding process for unwanted assets. Even where there are buyers, the current state of the world financial markets is such that there is no funding for business assets. This means that viable businesses within Australia are unable to secure bank funding for refinance purposes because of the international credit liquidity crisis. This places troubled companies, and therefore liquidators in performing their function, in an unusually poor situation.

Given the credit shortage for business purposes, liquidators have fewer choices than they usually have in a healthier market and therefore are unlikely to be challenged at this stage since much of the decision making is out of their hands. Nonetheless as the market improves, the decision to not carry on a business (even though valuations will continue to be difficult) will no doubt be scrutinised more closely than has historically been the case.

Liquidators must also undertake valuations for the purposes of recovering antecedent transactions. In these circumstances it may be that fluctuations in price might be used strategically by a liquidator to set aside transactions undertaken in a different set of market conditions. In particular the notion of an uncommercial transaction rests heavily upon a recognition of the benefits or otherwise of a transaction to the company.[29] In deciding whether a reasonable person in the company's circumstances would not have entered into a transaction regard must be had to the benefits both to the company and to other parties of entering into the transaction as well as the detriment to the company. Valuation of the assets involved in the transaction may be at the core of the dispute in these situations. [30]

Is it possible that in a rapidly falling market, transactions where parties sell an asset to the company may subsequently be attacked as being "uncommercial"? It is expected that both liquidators (and courts) are cognisant of the change in market conditions that may have caused an asset to rapidly lose its value. Nonetheless where asset and property transactions and values are examined and sought to be evaluated in hindsight it is sometimes difficult to see the basis of valuation for a particular item. As a result, liquidators may be in a more favourable position to pursue uncommercial transaction claims. Whether we see an increase in liquidator's pursuing uncommercial transactions is another matter entirely, given how busy the profession is at present, we postulate that there will be only slight increases in such actions and that they will be limited to the most obvious of cases (as they have been in the past).

---

[28] Section 477(2)(c)
[29] Similar valuation issues may also arise with respect to s 588FDA
[30] See *McDonald v Hanselmann* (1998) 28 ACSR 49; Morrison D. and Anderson C., "Uncommercial Transactions – Developments in the New Regime" (1999) 7 *Insolvency Law Journal* 184 at 190

Of the three types of administrations considered here, there may be less concern with valuation issues in liquidation than in a voluntary administration or a receivership. The liquidator has the obligation to realise the assets and hence can take the market as it happens to be at the time of the sale. There will be two key difficulties for the liquidator. The first will be where the asset or business cannot be sold, that will be a matter of fact although no doubt some liquidators will be questioned as to the extent that an effort was made to sell the asset and whether or not the sale was advertised widely enough. This will be a hurdle that is easily overcome for insolvency professionals in the current market although as mentioned above it is likely to be an issue as the market recovers.

Second, there is a real difficulty around the duty to preserve assets such as goodwill and the timing of asset sales. As noted above, the greater the commercial consideration associated with the relevant asset, the greater the need to respect the commercial nouse of the insolvency professional. Provided that reasonable care has been taken in determining asset preservation and the related timing of sale, it is our view that such decisions remain primarily within the domain of the liquidator. It would be unfortunate if courts were to take a more "hands on" approach in evaluating such decisions. Whilst the situation in *Hall v Poolman*[31] may be seen as a justifiable questioning of the liquidator's behaviour in a particular situation, it is suggested that if the decision is followed as an indicator of acceptable court interference, then it will be a dangerous development, especially in the light of current economic circumstances. Courts are ill equipped to make business decisions and there is a great amount of danger in assuming otherwise.

The administrator

The voluntary administration (VA) regime, contained in Part 5.3A of the *Corporations Act* (Cth) 2001, has at its heart the objective of salvaging a company's business when near insolvency or, if business rescue is not possible, to ensure a better return for creditors (and possibly members) than would otherwise result from an immediate winding up of the company.[32] The Part 5.3A provisions are a result of Australia's last major insolvency inquiry (the 'Harmer Report'),[33] one that favours the preceding English insolvency laws[34] by providing for a less restrictive way for the company to deal with external stakeholders in the event of business decline. The process of voluntary administration suggests that in most cases the administrator will attempt to continue the business in the short term. The administrator is given very broad powers to manage the company in this period. [35]However, as was shown above in relation to liquidation above, the rapid downturn in economic activity may see values decline so quickly that the administrator may be caught with little left to offer creditors as options for the company's future.

---

[31] [2007] NSWSC 1330 (2007) 65 ACSR 123 at [395]

[32] Section 435A *Corporations Act*

[33] Australian Law Reform Commission *Report number 45: General Insolvency Inquiry*, (ALRC 45, 1988)

[34] Report of the Cork Advisory Committee (Cmnd 6602, 1976), England

[35] See Divs 3 & 8 in Part 5.3A. The powers of the administrator to manage the company at this time were recognised by the High Court in *Patrick Stevedores Operations No 2 Pty Ltd v Maritime Union of Australia* [1998] HCA 30 at para52 per Brennon CJ, McHugh, Gummow, Kirby and Hayne JJ where their Honours stated that *"It is for the administrator, in the exercise of the discretionary powers conferred by s437A, to decide whether or not to carry on the company's business and the form in which it should be carried on during the administration."*

Because the administrator is appointed when there is a decline in the company's fortunes and because the administrator is required to act quickly, rapid diminutions in value might be best seen to be dealt with by an efficient process such as a voluntary administration. Nonetheless we may however see, *ex post* the lowest point of the market, suggestions that given unavailable credit, either the directors ought to have called for a voluntary winding up and/or security holders might have acted earlier and appointed a receiver to protect their assets in the light of credit difficulty. This kind of legal action will unfold in the future and is interesting to watch since most often the legal action follows the person with the deepest pockets. We are already witnessing actions against banks in a variety of circumstances and expect this to expand around external administration activity.

In any event, after appointment, the administrator in operating the business has the power to dispose of property subject to a charge, lien, or pledge or owned by another but in possession of the company, in the ordinary course of business.[36] It is suggested that where prices decline rapidly an owner or chargee of such property may question whether such a sale is in the ordinary course of business. This will be a difficult question to answer because the administrator will be required to demonstrate that the business was in fact being carried on and that in all of the circumstances it was viable for the purposes of the administration.

Section 439A requires the administrator of a company to convene a meeting of the company's creditors and to provide a report[37] setting out details of the company's business, property, affairs and financial circumstances. The report also requires the administrator's opinion as to whether the alternative outcomes of the administration are in the interests of creditors and the reasons for taking that view.[38] With respect to the financial circumstance aspect of the administrator's report, it will in current times be extraordinarily difficult to set out a reliable scenario for the company. The best that the administrator may do is to set out the financial circumstances as they are understood at that time. It is difficult to see how that judgement might be realistically questioned by a court at application stage or after the event. It seems clear that the administrator and their advisors will be play the key role in determining these issues and in the absence of foul play, those estimations of financial circumstance; however poor in hindsight will stand.

In the circumstance of the second creditors meeting, where a deed is accepted by the majority, a minority creditor will be in a good position since they will be able to challenge the decision more readily in a market where asset values are falling. A creditor can challenge the deed under s 445D on the two grounds. First, that the administrator's report was misleading because it did not anticipate a decline in value or second, a challenge may be made on the basis that effect cannot be given to the deed without injustice. In circumstances where there is an expectation of continual decline in economic activity, the administrator will include that estimation in the report.

Given the role of heightened uncertainty in capital markets at present, administrators are most likely presenting a dim view of viability and prospects in their reports. It is difficult to imagine, at

[36] Section 442C
[37] Section 439A(4)
[38] Section 439A(4)(b) where that outcome is one of three possibilities: a deed of company arrangement, to bring the administration to an end, or to wind up the company

a general level, there being much optimism for administrators preparing reports at this time. Whilst history suggests that the economy will recover, this downturn has economic commentators at odds over the extent of the cycle (whether or not Australia is in recession) and also as to when the economy might recover. An administrator faced with a failing company in a difficult economy will certainly be wary of bold predictions or outlook when making recommendations to creditors the second meeting. We therefore expect to see an increase in administrator recommendations for winding up at the second creditors meeting.

The Receiver [39]

A receiver's powers depend upon the basis of their appointment. Specifically it is necessary to examine the instrument that appoints the receiver.[40] Usually the agreement between the company and the secured creditor gives wide powers to the receiver to ensure that the chargee has the capacity to protect their asset in the event of a default. The circumstances of default are usually defined widely and often include a reference to financial ratios that consequently has valuation implications. Where for example an agreement requires that a debt to asset ratio be maintained at a certain level, default is triggered where the asset value declines sufficiently.[41] In the current economic environment lenders are likely to be examining the value of assets held as security in conjunction with the satisfactory payments by debtors of debt obligations. It is important to note however that if the agreement provides for a trigger when asset values decline, then the debt may be called notwithstanding the otherwise exemplary behaviour of the borrower.

A further clause often found in such instruments is the requirement for the borrower to submit (usually audited or externally prepared) accounting records on a regular basis.[42] One of the key comments made by courts when reporting on the solvency of a debtor is the inadequacy or lack of accounting records. We believe that lenders in seeking to best manage current liquidity difficulties will seek to enforce more closely such clauses as part of their overall risk assessment of debtors.

Aside from the private arrangements made between parties the *Corporations Act* also provides for a wide range of powers, see s 420 of the *Corporations Act.* The powers hold provided they are not inconsistent with the appointment instrument. The statutory powers are similar to those held by other external appointments and allow for the carrying on of a business[43] and for the disposal of property.[44] It therefore follows that the challenges as outlined above around asset values and prospects are apparent for the receiver when appointed.

[39] In this section we use the term receiver to cover receiver and receiver and manager. The discussion is limited to a private appointment rather than one made by a court

[40] *Inglis Electrix Pty Ltd v Healing (Sales) Pty Ltd* [1965] NSWR 1652

[41] This is similar to margin loans for share and securities trading where the amount that the lender is prepared to advance is entirely dependent upon the value of the securities. As the value of the security charged fluctuates so too may the advance credit rise (where the value of a security increases) or fall triggering a call upon the borrower chargee where the value of the security declines past the limit implied by the operation of the ratio of debt to asset value

[42] The regularity required for the submission of accounts is a function of the perceived risk on the part of the lender. Quarterly or annual reports are not unusual in this context

[43] Section 420(2)(h)

[44] Section 420(2)(g)

Unlike administrators and liquidators, who owe their duty to all creditors; at common law the receiver is able to give preference to the secured creditor who made the appointment.[45] It logically follows that a receiver is most likely to allocate their priorities in such a way since they have been appointed pursuant to a charge held by the chargee. At common law, receivers in Australia only have the duty to act in good faith;[46] however the legislative additions effectively increase the duty of the receiver. Specifically, section 420A makes clear the fiduciary aspect of selling the property of the company to ensure a reasonable price on sale.[47]

There is confusion about the precise limits of s420A because it is not immediately clear how the notion of "market value" might differ from the requirement of "best price". If the two were to differ, it is difficult to see how a receiver, or indeed an expert valuer, might reasonably explain the difference. In *Skinner v Jeogla Pty Ltd* [48] Spigelman CJ stated[49] that the two paragraphs in s 420A(1) "*are intended to be both exhaustive and mutually exclusive*". The emphasis to be apparently placed on the word "otherwise"[50] indicates that its meaning suggests some property is capable of being sold even though it does not have a market value.[51] Thus the receiver has to comply with either paragraph (a) or (b) when selling the company property. Where the property has a market value, the receiver must take all reasonable care to sell the property for not less than that price. If the property does not have a market value, the receiver must take all reasonable care to sell the property for best price obtainable having regard to the circumstances. The "market price" is, according to Spigelman CJ in the *Skinner case*, to be found in the situations where there is a definite price or a "*clearly and obviously established market price*"[52] or it has a determinable value because of *"number and nature of comparable sales"*[53]. On the other hand, if property is *"so unique"* that *"comparisons cannot readily be made, or it is so scarce that sales are rare"*[54] then it may fall into the category where s 420A(1)(b) applies. This view appears to have been accepted by some but not all of the subsequent cases.[55] The position facing a receiver seeking to comply with s 420A, on this basis, seem to be that they must determine if there is a market price and then take reasonable steps to meet that price at sale. If there is no such price, then the receiver ought to take steps to get the best price that is reasonably achievable.

---

[45] *Expo International Pty Ltd v Chant* (No 2) (1979) 4 ACLR 679

[46] *Pendlebury v Colonial Mutual Assurance Society Ltd* (1912) 13 CLR 676; *Expo International Pty Ltd v Chant (No 2)* (1979) 4 ACLR 679

[47] Section 420A(1) states that "in exercising a power of sale in respect of property of a corporation, a controller must take all reasonable care to sell the property for" either the market value or otherwise if there is no market value for the best reasonable "having regard to the circumstances when the property is sold"

[48] [2001] NSWCA 15

[49] At [33]

[50] Footnote 47 sets out the relevant wording of the provision

[51] The view set out in Skinner v Jeogla Pty Ltd has been followed by Bryson J in *GE Capital Australia v Davis* (2002) 150 FLR 250 and *Deangrove Pty Ltd v Buckby* (2006) 56 ACSR 630.

[52] At [39]

[53] At [40] where Spigelman CJ referred to this as a "determinable value"

[54] At [40]

[55] See Bryson J in *GE Capital Australia v Davis* (2002) 150 FLR 250 at 284. However a contrary view seems to have been expressed by Young CJ in *Ultimate Property Group Pty Ltd v Lord* (2004) 22 ACLC 423 at [95] –[105]

Whilst the interpretation in *Skinner* enables the section to be given effect, it does strain the general conception of 'market value', both in its commercial useage and as compared with established case determinations in other contexts[56]

If one accepts the interpretation of Spigelman CJ, it seems that in the context of difficult market conditions the ability to use "comparable sales" type approach will be diminished as the prices obtained will be very different from earlier sales in more buoyant economic times. If there is a widely recognised record of prices (such as on a stock exchange) then it will of course be possible to identify the decline in prices, however this probably only caters for a small part of the market.

For both limbs of s420A it appears to be critical that the receiver adheres to certain processes in conducting the sale so as to establish that they have fulfilled the respective requirements.[57] Initially the receiver must identify the property and take steps to identify the appropriate market for it. This seems to apply to both limbs of s 420A. If there is a market value as under (1)(a) then it is necessary to know what the market is before one can be said to be able to ensure that reasonable steps have been taken to get the market price. Alternatively in (1)(b) the best price reasonably obtainable may only be achieved if it is in the right market. As made clear in the *Jeogla* litigation, if there is a lack of care such that the market for the asset is incorrectly identified, then such failure will almost certainly be seen as a breach of the section.[58]

Once the market is identified, the receiver is required to advertise in a way that will bring the property to the attention of the relevant buyers; [59] a difficult task in present climes. The question of whether the advertising is adequate ought not be critical in examining receiver behaviour since the main purpose of the receiver is to get a proper price. As stated by the Victorian Court of Appeal in *Vasiliou v Westpac Banking Corporation & Ors*: [60]

> By itself, the presence, or absence, of advertising will rarely be decisive. What matters is the price obtained. If the price is satisfactory, a failure to advertise will be immaterial.

Adopting the view that pursuant to s 420A(1)(a) a receiver must reasonably seek to reach a "market" price that is clearly identifiable or readily identifiable, then if that price was obtained without advertising, the duty has been fulfilled. On the other hand it seems difficult to imagine a situation where the receiver might be said to satisfy s 420A(1)(b) without appropriate advertising. Where the item to be sold is unique or has no trading comparison it seems it is for

---

[56] See *Emerson v Custom Credit Corporation Ltd* [1994] 1 Qd R 516; Fisher R., "What is a Receiver's Duty when Selling Assets" unpublished paper presented at *Insolvency Law Workshop* Queensland University of Technology, Brisbane, 11 July 2008

[57] See O'Donovan *Company Receivers and Administrators* (Lawbook Online, Sydney, 2009) [11.2130] where it is stated that *" In this sense, Corp Act, s 420A is about the process, not the result."* This being based on the fact that the receiver must "take all reasonable care" to either get the market value or the best price in the circumstances as the case may be. It is not clear if the failure to achieve the appropriate price can satisfy the section without any reasonable care: see *Artistic Builders Pty Ltd v Elliott & Tuthill (Mortgages) Pty Ltd* [2002] NSWSC 16 but this was questioned by Young CJ in *Ultimate Property Group Pty Ltd v Lord* (2004) 22 ACLC 423

[58] *Jeogla Pty Ltd v ANZ Banking Group Ltd* [1999] NSWSC 563 ;(1999) 150 FLR - although on the leave to appeal per Spigleman CJ. at [42] suggested that the facts in the case had not been applied to s 420A(1)(b) by Einstein J at first instance

[59] *Commercial and General Acceptance Ltd v Nixon* (1981) 152 CLR 491 [

[60] [2007] VSCA 113 at [62] per Maxwell P, Neave and Kellam JJA

the receiver to test the market to ensure that they are able to justify their selling price. It may be therefore necessary to recognise that there may be some difference as to the advertising requirements where the property has a market value as compared with where the property does not have a market value. However, applying s420A(1)(a), from a policy perspective, if the goal of s420A is to ensure that receivers make reasonable endeavours to get the *best* price for the assets of the company it is difficult to accept that a sale need not be advertised amongst potential buyers. There must be limits as to what is expected in advertising in that a reasonable limit must be imposed on the extent of the advertising. In terms of the Victorian Court of Appeal approach in this area the difficult question is how the receiver or the court determines if the price may be considered "satisfactory" if potential buyers were not aware of the sale. In difficult market conditions it may require the receiver to advertise more widely to ensure that care taken is reasonable. The very real practical difficulty for most receivers is that they cannot be certain that additional expense is justified in terms of potential increased returns. Another area of concern is the lack of clarity over who may enforce the section. It would take little effort to place in the section a clear statement of the parties entitled to pursue action against the receiver and or the receiver's appointor.

The wording in s420A remains problematic to say the least. Whilst it is likely there will always be conflict between the secured creditor and the debtor in the case of a forced sale of the debtor's property in these circumstances, it is possible to at least clarify the obligations of the parties' in terms of the receiver's duty. The inappropriate wording should be remedied to remove either paragraph (a) or (b). The section would be much clearer if there was a simple statement that the receiver must take all reasonable steps to ensure that the assets are sold for the best price in the circumstances. The current difficult economic conditions will only serve to highlight the section as secured creditors act to protect their interest and debtors seek to strategically protect themselves against claims.

Conclusion

The impact of the global financial crisis has yet to fully play out in the context of external administration activity. As the fall-out takes a hold in the end process for near-insolvent and insolvent businesses we will better know the tensions that exist around the effective operation of the relevant *Corporations Act* provisions. The concern addressed is that the various regulatory rules and case law interpretation of those rules have developed in times of relative well-being and stable asset prices. This has made the end game at least somewhat predictable.

This paper examined the likely impact of the general decline in economic outlook within Australia upon the increasing number of corporate reorganisations, rescues and insolvencies. We believe that the significant decline in economic health within the Australian economy will provide the first real test of the current *Corporations Act* insolvency provisions since they were introduced in June 1993.

Specifically the paper considered the likely impact in valuation terms and addressed some of the more likely immediate concerns for insolvency professionals. We take the view that whilst there are some trouble spots, that generally Australia's corporate insolvency provisions are in good shape to handle the more severe forthcoming economic conditions.