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LAWYERS & NOTARIES

Deregistration and Winding up of Australian Companies

Introduction

There can be a number of legal and commercial reasons to end the life of an Australian company. While the most obvious and common reason remains the insolvency of the company, business restructuring, merges, consolidations, sale of business, and even retirement of the principals are examples of reasons why a company's life is to be terminated. On such an event, the assets of the company are distributed among the creditors of the company and, if there is, any surplus assets remaining after such distribution, to be returned to the shareholders.

Deregistration of a company in Australia is a relatively simple and inexpensive process. Either a company can be deregistered directly if certain conditions are met, or deregistration will follow after a winding up, or liquidation, of the company.

In addition to deregistration and liquidation, there are a number of other forms of external forms of administration of the affairs of the company, such as receivership or administration, which occurs only in certain circumstances when the company is insolvent. These processes exist to either protect and enforce the rights available to a secured creditor or to ensure that there is an orderly and equitable distribution of the assets of an insolvent company among the same class of creditors, instead of allowing for a free-for-all where the ability of a creditor to recover their debt is held hostage by timing, bargaining power, and resources.

Deregistration of a Company

The existence of a company is independent of the business that it undertakes; even if a company has ceased business operations, the company remains in existence until it is deregistered. As such, it will continue to have ongoing obligations under the *Corporations Act 2001* (Cth) (the "Act") and other relevant laws. These obligations include the continuing maintenance of financial and company records, payment of annual review fees, reporting requirements, as well as taxation obligations. Accordingly, if there is no more need for the existence and continuing maintenance of a company, the company is neither insolvent nor in financial difficulties, and there is no incentive for the company's continued existence (such as accumulated losses that may be offset against future earnings), it ought to be deregistered.

Deregistration itself, if the shareholders of the company in general meeting have unanimously resolved to do so, can be as simple a process as lodging a form with the Australian Securities Investments Commission ("ASIC"). This option is available only if the following legal requirements are met:

- all the shareholders agree to the deregistration;
- the company is no longer carrying on business;
- the company's assets are worth less than $1,000.00;

- the company has no outstanding debts, liabilities, payment obligations, etc. towards its employees, including leave entitlements and superannuation benefits;
- the company is not a party to any court proceedings; and
- the company has paid all outstanding fees and any penalties payable under the Act.

Any application for deregistration of a company must be accompanied by a declaration by the directors to the effect that all of the requirements are met. In the event that the company's assets exceed $1,000.00 after payment of its liabilities, these assets must be reduced to less than the maximum threshold through various means, such as the payment of a special dividend or a share buyback, before deregistration can occur.

If the application is determined by the ASIC to be compliant with the law, notice of the proposed deregistration would be published on its website. Following two months of there being no objections lodged with the ASIC for deregistration of the company, the company would then be deregistered.

Members' Voluntary Winding Up of the Company

If the prescribed criteria for direct deregistration of a company cannot be met and yet the company is solvent, the company must be wound up or liquidated prior to deregistration. Commonly, this is done by way of a "members' voluntary winding up", where the shareholders of the company simply resolve in general meeting by special resolution (i.e. with a 75% majority of those present and voting) that the company be wound up and a liquidator be appointed. The appointed liquidator is charged with the responsibility of paying out all debts of the company, paying a dividend of any surplus assets of the company to the shareholders, and then deregister the company.

This process is regulated by Section 495 and other related provisions of the Act.

Creditors' Voluntary Winding Up of the Company

In the event that the company is insolvent and the directors of the company are not resistant to the prospect of the company being placed in liquidation, there can be a voluntary winding up in insolvency where, after the shareholders decide to wind up the company, it is the creditors and not the shareholders to whom the liquidator would be accountable.

The principal difference between a "members' voluntary winding up" and a "creditors' voluntary winding up" is that, because there are insufficient assets in the company to meet all debts and liabilities, it is the creditors and not the shareholders that will supervise the process of the winding up, so that the dissolution of assets can be done equitably in their interest rather than those of the shareholders or directors.

Otherwise, the process of a creditors' voluntary winding up is similar to that of a members' voluntary winding up. The liquidator would take over control of the company and the administration of its affairs, terminate the employment of any employees, identify and pay the debts and liabilities of the company, and proceed to deregister the company with the ASIC. Where the company is insolvent, as is the case of a creditors' voluntary winding up, the costs and expenses of the liquidator have first priority to the assets of the company, followed by those of the employees (there are a number of exceptions, such as those employees who are also directors of the company).

Court-Ordered Liquidation of a Company

In addition to the voluntary winding up processes, there is the option available for an application to be made to either the Federal Court of Australia, or the Supreme Courts of the States and Territories for a company to be wound up by an order of the Court.

The most common reason for a court-ordered winding up is that the company is insolvent and, in such circumstances, a creditor, director, or even the company itself may apply to a court under section 459P of the Act for a company's winding up. Either in the alternative or in addition to the insolvency of the company, there are also certain circumstances where a court can order the winding up of the company under section 461 of the Act, such as where a company has no shareholders, the directors and/or shareholders of the company cannot agree as to the conduct of the affairs of the company, or where the directors of the company have been found to be conducting the affairs of the company to further their own interests rather than that of the company.

In the case of a court order for liquidation of the company, the liquidator is appointed as an officer of the court and is thus responsible to the court for the administration of the winding up. Otherwise, the process of the liquidation is similar of that of a voluntary winding up, where the liquidator would take control of the company, pay out the debts and liabilities of the creditor to the extent that it can, and deregister the company.

It is not unusual in the case of a court-ordered winding up, that the liquidator would want to investigate the past affairs of the company that led to its insolvency, though a liquidator in a voluntary winding up can do so as well. In particular, the liquidator would investigate, to the extent that available funds allow, whether:

- the directors have been trading the company while insolvent;
- payments have been made to certain creditors in preference of other creditors, a payment that is referred to under section 588FA of the Act as a "unfair preference";
- whether transactions have been entered into by the company with the effect that valuable assets of the company are transferred out of the company for nil or insufficient consideration, which is called a "uncommercial transaction" in section 588FB of the Act; and
- any other breaches of the duties of the directors to the company, in particular, but not limited to those provided under sections 179 to 184 of the Act, such as the duty to act honestly, in good faith, and in the best interests of the company.

In the event that such investigations reveal that proceedings may be brought by the liquidator against preferred creditors, recipients of company assets, and/or the directors' company for remedies that usually involve the payment of compensation to the company that would then be distributed among the creditors of the company after deducting the necessary amounts for costs.

In the case of most companies, there would be insufficient funds in the company for the liquidator to undertake full-scale investigations and contributions from creditors are often called for in either funding such investigations or to undertake proceedings to recover assets or damages for the creditors. It has also become increasingly common for liquidators to consider entering into funding arrangements with third party litigation funders that would provide such funding for investigations and court proceedings in return for a share of any proceeds recovered against the prospective defendants.

As with the case of voluntary winding up, a court-ordered winding up would ultimately end with deregistration of the company.

Other Insolvency Processes

Two of the other more common forms of external administration of insolvent companies are receiverships and administration.

Where a company has obtained funds advanced to it by a financier that is secured by assets of the company, on the default of the loan terms or the insolvency of the company, the secured creditor may enforce their rights by appointing a receiver, receiver and manager, or controller, to the assets that have been pledged as security. Common forms of such security include hire purchase mortgages and fixed charges, of which the security relates to a particular asset, such as land, a vehicle or heavy equipment, or a "fixed and floating charge" over the entire business undertaking of the company. These security instruments are now required to be registered under the *Personal Property Securities Act 2009* (Cth).

The appointment of a receiver, controller, or receiver and manager to one, more, or all of the assets of the company does not affect the existence of the company itself. It is often the case that, if the entire business undertaking of a company is placed in receivership, the company itself would then be placed in liquidation. While at first glance this may appear to be an unnecessary duplication of processes and resources, it must be kept in mind that a liquidator may recover assets or damages from directors and third parties, such as in the event of insolvent trading, which are avenues of recovery that are not available to receivers and thus there may still be some property available for distribution among creditors. Further, a receiver, receiver and manager, or controller is accountable to and required to act in the best interests of the secured creditor that appointed them, whereas a liquidator is accountable and responsible either to the creditors of the company and/or the court.

In an administration, either the directors of a company or a secure creditor who has security over the entire business undertaking of the company may choose to appoint an administrator to the affairs of the company where the company is insolvent. The administration process is based loosely on the chapter 11 process in the United States that is designed, in the case of Australian law, to provide an insolvent company with a brief respite to review its financial position, identify all of its debts and liabilities, identify assets available for distribution, and consider the best process forward. Usually, an external administration process would last for no more than one to two months.

On appointment, an administrator takes over control of the company and all existing court processes against the company are suspended. After a brief overview of the financial position the company, the administrator would convene a meeting of the creditors of the company with a view to deciding the company's future. These options usually are:

1. returning control of the company to its directors;
2. to put the company in liquidation; and
3. for the company and its creditors to enter into a "Deed of Company Arrangement" ("DOCA").

A liquidator would recommend to the creditors that the company be returned to the control of the directors of the company if and only if the company is in fact solvent or has in fact become solvent in the course of the administration.

In the event that the company is insolvent and is unlikely to be able to trade out of its difficulties, the company may be placed in liquidation. If the creditors so decide, the process would automatically be converted to a creditors' voluntary winding up and the appointed administrator would automatically become the liquidator unless the creditors of the company decide otherwise.

Where the company has real prospects of being able to trade out of its difficulties, the directors or a third party purchaser, which may be a creditor, may make a proposal to the creditors for a DOCA. Common terms that may be found in a DOCA include capital injection into the company, conversion of some of the debts of the company into equity, changing the composition of the board of directors, change in the shareholding of the company, and a prescribed percentage and timing for payment of dividends to unsecured creditors. For example, a company with debts of $1 million to its unsecured creditors may find it appealing to accept a proposal from one of the major creditors, holding $500,000.00 of the debt, to convert its debt into a substantial majority of shareholder or even the sole shareholder of the company, provided that that shareholder invests, say, $150,000.00 over six months into the working capital of the company and that the other unsecured creditors are paid 20% of their debts within twelve months in full and final settlement of their debts against their company.

The principal reason why such DOCAs may be found appealing by the creditors is that they are persuaded by the liquidator as well as their own advisors that, in a hypothetical liquidation taken place on that day, they would receive substantially less than what is being offered under the proposed DOCA and, if the company is allowed to trade out of its difficulties, each of the creditors may well retain a continuing trading customer. The consideration of such DOCAs, without the administration process, would previously have been impossible under either a voluntary winding up or a court-ordered winding up process.

Further Information

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