



ASIC

Australian Securities & Investments Commission

REPORT 129

Review of s439A reports for voluntary administrations

June 2008

About this report

Voluntary administrators are required to prepare a report under s439A of the *Corporations Act 2001* (Cth) (Corporations Act) to enable creditors to make an informed decision about the future of the company under administration.

ASIC has reviewed a number of these reports against the requirements in s439A, taking into account case law and industry guidance. This report presents the findings of our review.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

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

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report presents general findings. The criteria used for ASIC's review of s439A reports are based on statutory requirements, case law and industry guidance as they stood at the time of the review and as interpreted by ASIC. No part of this report or its contents is intended as legal advice or a comprehensive instruction on how external administrators must act in order to comply with their obligations under the Corporations Act.

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Executive summary

Role of voluntary administrations

Since its introduction in 1993, the voluntary administration procedure has become a frequently used type of external administration.

It allows the business, property and affairs of an insolvent company to be administered in a way that maximises the chances of the company, or as much as possible of its business, continuing through a deed of company arrangement (DOCA) or that results in a better return for the company's creditors than an immediate winding up.

The important decision about whether or not to accept a proposal for a DOCA falls to the company's creditors. In making this decision, the creditors rely heavily on the independence, competence and professionalism of the administrator to present them with information and advice so they can make a fully informed decision on the future of a company in which they are financially involved.

This decision on the future of a company is underpinned by an adequate investigation by the insolvency practitioner (the administrator) about the company's business, property, affairs and financial circumstances. Armed with the results of that investigation creditors should be able to make an informed decision on whether to accept a proposed DOCA or to wind up the company.

Size and focus of our review

We looked at 275 reports prepared by administrators for companies that entered into voluntary administration between 1 July 2006 and 15 March 2007 when the administration resulted in a DOCA. We assessed the reports against:

- a standard based on statutory and case law requirements¹ as well as
- guidance that the Insolvency Practitioners Association (IPA) mandates for its members²

Our review focused on assessing the reports to determine if sufficient information was given about the company's business, property, affairs and financial circumstances so that creditors could be fully informed when deciding whether to either:

- accept the DOCA proposal or
- place the company into liquidation.

¹ See Appendix 1 of this report for a summary of the main statutory requirements under the Corporations Act

² 'Statement of Best Practice—Content of an Administrator's Report Pursuant to Section 439A(4) of the Corporations Law' effective 1 July 2001 (IPA Statement of Best Practice). The IPA is currently reviewing its guidance on the preparation of s439A reports and has issued a revised s439A guide for consultation.

Key findings: Practitioners need to improve their reports

Many reports failed to give creditors enough information about the company's business, property, affairs and financial circumstances to enable them to make a fully informed decision on whether it would be better to vote to:

- accept the DOCA proposal or
- place the company into liquidation.

This finding follows from our assessment that most reports failed to give enough information to indicate that an adequate investigation had been carried out given the size and nature of the business conducted by the company.

Our review leads us to the conclusion that for the majority of reports, administrators either did not:

- undertake an adequate investigation or
- fully report to creditors on the results of that investigation.

Each individual creditor makes a commercial decision regarding a DOCA proposal. The absence of the required information will impact the ability of creditors to make a fully informed decision. However, this does not necessarily mean that, if the information had been provided, individual creditors or creditors as a group would have made a different decision on any particular DOCA proposal. The failure to provide adequate information does, however, increase the risk of this decision for creditors.

Because conducting an investigation and reporting to creditors on the results of that investigation is the basis of the statutory requirement placed on administrators, our key findings indicate that practitioners need to improve their practices in the preparation of s439A reports.

Other requirements were generally met in most reports.

Recommendations: Eight suggested key improvements

Creditors need relevant information when deciding on an appropriate commercial outcome. They have to collectively decide between accepting a DOCA proposal or voting to place the company into liquidation.

Our review identified the following key improvements to reports that would help creditors become fully informed when making decisions. Areas of improvement that are relevant to the circumstances of a particular voluntary administration depend on the omissions of the administrator in preparing that specific report. The results of our review highlight omissions compared with

a standard. Our conclusions are based on omissions that carry the risk of adversely impacting the ability of creditors' to make a fully informed decision. Omissions on each of the matters discussed in the following table may be material in the context of a particular report or it may be a combination of factors before there is a risk of an adverse impact on creditor decision-making.

Eight suggested improvements for preparation of s439A reports for creditors

1 Reporting on company history and reasons for failure	When the DOCA outcome depends on the success of future trading, some analysis and explanation of the history of the company and the reasons for failure identified by the practitioner would benefit creditors in their decision-making.
2 Analysis of financial results	Providing a proper understanding of the past financial results would support creditors' understanding of the company's future prospects when a DOCA proposal includes future trading.
3 Validation of related party claims	An assessment of related party claims and better disclosure of the administrator's opinion on the legitimacy of the related party claims would promote creditor confidence on DOCA proposals. It would also allow creditors to make an informed assessment of the impact of related party claims on the proposal.
4 Future trading assumptions	Creditors making a decision on a DOCA proposal involving future trading would benefit from information on: <ul style="list-style-type: none"> • the administrator's views on future trading projections; • the assumptions underlying the projections; and • the likelihood of the terms of the DOCA proposal being achieved.
5 Reporting on potential recoveries in a liquidation	Creditors need to consider a DOCA proposal in light of the possible returns from a liquidation. Creditors need more information about: <ul style="list-style-type: none"> • possible returns from recovery actions only available to a liquidator; and • any likely realisations from those actions.
6 Comparison of returns	It is useful for creditors if estimated returns from a DOCA and liquidation are presented, as far as possible, on a comparable basis. When ranges are used creditors can be given more information on the factors that will influence an outcome towards the high or low end of the estimated recovery range.
7 Extending the convening period	Administrators should consider adjourning the second meeting of creditors or extending the convening period when they have been unable to finalise their investigations because they have not received all of the company's books and records. This will allow them to give enough information to creditors to allow them to make a fully informed decision.
8 Clear reporting	Creditors are entitled to a report that is clear, concise and informative. Administrators should endeavour to: <ul style="list-style-type: none"> • make complex issues easier for creditors to understand; • provide information that is relevant to the company's circumstances and tailor standard reporting templates to avoid providing bulky and unnecessary background information; • avoid repetitious, generic information which is of limited use, if any, to creditors in making decisions; • avoid jargon; and • use plain English.

Future ASIC action

This review gives feedback to the corporate insolvency industry about preparing s439A reports. Recent amendments to the Corporations Act also clarify some of the matters discussed in this report.

We:

- are bringing the contents of this report to the attention of practitioners so they, and the IPA, can address the findings through improvement of their practices and industry guidance;
- will be paying particular attention to s439A reports as part of our future compliance work; and
- are intending to conduct a further review at a future time to assess whether there has been an increased standard of compliance.

We will be working with the industry to ensure improved compliance and will take further action if we become aware of continued deficiencies in s439A reports. Following recent insolvency law reform we now have standing as an applicant under s445D of the Corporations Act to seek to have a DOCA terminated by the court in certain circumstances.

A Details of the review

Key points

An administrator in a voluntary administration must investigate and report to creditors about the company's business, property, affairs and financial circumstances.

Our decision to review s439A reports resulted from liaison with the corporate insolvency profession and was co-ordinated by our Liquidator Compliance Unit.

We reviewed 275 reports against a standard based on:

- statutory requirements;
- the interpretation of these requirements in relevant case law; and
- mandatory guidance in the IPA Statement of Best Practice³.

Background to the review

The Corporations Act requires an administrator in a voluntary administration to investigate (s438A) and report to creditors (s439A) about the company's business, property, affairs and financial circumstances. These provisions are connected as the administrator's report is based on the investigation. Indeed, the purpose of the investigation is to ensure that the administrator 'is in a position to put informed recommendations' to the creditors.⁴

Since its introduction, the practical operation of the voluntary administration procedure has been reviewed on several occasions.⁵ The law relating to voluntary administrations was amended through the *Corporations Amendment (Insolvency) Act 2007* and the Corporations Amendment Regulations 2007 (No 13), which took effect on 31 December 2007. These amendments were not in place at the time we undertook our review. However, they are relevant to our future activities and are discussed in this report under the heading 'Future Action'.

Purpose and scope of the review

The decision to review s439A reports arose from our liaison with the corporate insolvency profession. The purpose of the review was to test compliance with legal requirements and mandatory industry guidance. The

³ Following this review the IPA has issued revised guidelines

⁴ Corporate Law Reform Bill 1992, *Explanatory Memorandum*, paragraph 496.

⁵ This includes a 1998 ASIC study, which focused on the conduct of 55 administrations conducted by 16 practitioners from metropolitan Sydney; reviews by the Companies and Markets Advisory Committee in 1998 and 2004; and an evaluation as a part of the Parliamentary Joint Committee for Corporations and Financial Services report on *Australia's Corporate Insolvency Laws: A Stocktake* (2004).

review focused on situations where creditors were asked to consider a DOCA proposal and decided to accept that proposal. In these situations, creditors are very dependent on the information provided to them by the administrator in a s439A report to enable them to make an informed decision about the company's future.

Our intention in carrying out the review and releasing our findings is to inform stakeholders and to promote the outcome that creditors are provided with sufficient information to enable them to make an informed decision about the future of the company, if called on to do so. We do not intend to take enforcement action based on any of the findings of this review as this review was designed to test the standard of reporting and raise awareness of any deficiencies. However, in future cases, we will consider all available options where we are of the view that creditors have not been provided with the requisite information to support their decision-making.

ASIC's role and related activities

The review was co-ordinated by ASIC's Liquidator Compliance Unit (LCU). LCU was set up in early 2006 to influence the behaviour of registered liquidators to maintain high standards of competence and integrity. Public confidence in the competence and integrity of registered liquidators is essential to support a credible corporate insolvency system within a well-functioning market economy.

The review was carried out against the background of a revision by the IPA of industry guidance for registered liquidators on complying with their legal obligations, including guidance on the administrator's report to creditors.

ASIC's other work with the corporate insolvency profession includes:

- registering liquidators;
- helping liquidators get co-operation from corporate officers in external administrations;
- acting on reports lodged with us by administrators and liquidators of likely offences;
- receiving, recording and maintaining a record of all statutory lodgements by liquidators;
- funding liquidators under the Assetless Administration Fund to complete reports on possible contraventions of the Corporations Act;
- publishing a series of information sheets for creditors and others involved in the insolvency process; and
- through the National Insolvent Trading Program, intervening early when companies are possibly insolvent.

Criteria for sample selection

For this review, we looked at reports for all voluntary administrations that:

- started between 1 July 2006 and 15 March 2007; and
- resulted in acceptance by creditors of a DOCA that was executed before 2 April 2007, even if the company was subsequently placed into liquidation.

1680 voluntary administrations started during the chosen period: see Table 1. Of these administrations, 275 (or 15.8%) resulted in a DOCA: see Table 2. Of these DOCAs, 18.6% subsequently resulted in a liquidation (up to 31 December 2007).

Table 1: Geographical spread of voluntary administrations

Region	No of administrations	% of total administrations
NSW/ACT	716	42.6%
VIC/TAS	411	24.5%
QLD	391	23.3%
SA/NT	93	5.5%
WA	69	4.1%
TOTAL	1680	100%

Table 2: Geographical spread of DOCAs

Region	No of DOCAs	% of total DOCAs
NSW/ACT	152	55.3%
VIC/TAS	43	15.6%
QLD	46	16.7%
SA/NT	16	5.8%
WA	18	6.6%
TOTAL	275	100%

The 275 reports we reviewed for these DOCAs were prepared by, on or behalf of, 174 different administrators: see Table 3. Fifty-four percent of the administrations were joint appointments involving two or more administrators. The administrators were partners or employees of 80 different firms. Twenty-nine reports related to the affairs of corporate groups. Of the 174 administrators, 154 (89%) were members of the IPA. Table 4 and Table 5 set out the estimated costs and returns as reported to creditors.

The ranges used in Tables 4 and 5 are the same used by ASIC in collecting statistics from reports lodged under s533, 422 and 439D of the Corporations Act.

Table 3: Type of firms preparing the reports

No of sole practitioners	No of firms with 2–4 liquidators	No of firms with 5 or more liquidators	Total no of firms
25	35	20	80

Table 4: Estimated costs (% of reports in each range)

Range of costs	For voluntary administration	For liquidation as an alternative to DOCA
\$0	0%	0%
\$1–\$50,000	76%	67%
\$51,000–\$100,000	11%	15%
\$101,000–\$250,000	3%	6%
\$251,000–\$500,000	8%	1%
Not provided	2%	11%
TOTAL	100%	100%

Table 5: Estimated returns (% of reports in each range)

Range of returns (cents in the dollar)	For proposed DOCA	For liquidation as an alternative to DOCA
0	9%	68%
1–10c	30%	11%
11–20c	19%	7%
21–50c	18%	4%
51–100c	18%	3%
Not provided	6%	7%
TOTAL	100%	100%

How the reports were assessed

Information requested

For each voluntary administration included in the sample, we asked the administrator to provide the following information:

- the report as to affairs (if provided by the directors of the company);
- the initial circular to creditors advising of the administrator's appointment;
- the initial and any subsequent reports to creditors under s439A(4);
- any additional report or other documentation presented at a meeting of creditors held under s436E or 439A; and
- the minutes of the first and second meetings of creditors.

Our review was based on the information received.

The assessors

The material was allocated among our staff with at least seven years' experience at a senior level gained from previously working in the insolvency profession.

The assessment process

The guiding rule

The purpose of the s439A report is to give creditors sufficient information to enable them to make an informed decision about the options available to a company under administration. The guiding rule for the adequacy of a s439A report is whether it gives creditors the requisite information.

The standard

The Corporations Act provides little guidance on the content of the s439A report.⁶ The case law provides some general principles. Ultimately, the administrator must use professional judgment in preparing the report. The IPA Statement of Best Practice provides guidance to assist administrators with this task.

In our review, the reports were assessed using a purpose-built assessment tool. This was developed to ensure that an objective assessment could be made against the standard. The standard consists of:

- statutory requirements;
- the application of case law principles – but only to the extent that those principles set a standard that could be measured objectively; and

⁶ See Appendix 1 of this report for a summary of the main statutory requirements.

- mandatory guidance provided in the IPA Statement of Best Practice.

The IPA Statement of Best Practice includes three categories of guidance—matters that an administrator:

- *shall* include in the report to creditors;
- *should* include in the report to creditors; and
- *may* include in the report to creditors.⁷

Although our assessment covered both the ‘*shall*’ and the ‘*should*’ guidance, the findings in this report are limited to guidance that the IPA regards as mandatory for its members (i.e. the *shall* guidance).

The criteria for the review take into account that the actual contents of a s439A report depend on the circumstances of the particular external administration. In our application of the standard, we took into account that the extent and nature of reporting is necessarily affected by the history, size and complexity of the affairs of the company being administered.

Additional comments to assist with the further development of guidance

We are aware that the IPA is currently revising its guidance. Therefore, in addition to reporting the findings against the standard, we also include comments we hope will provide a useful contribution to that process.

The assessment criteria

Table 6 summarises the criteria used for assessing each report and how they relate to the standard.

Table 6: How the assessment criteria relate to the standard

Criteria	Key question	Key aspects of the standard ⁸
Quality of investigation	Did the administrator conduct an adequate investigation (as reviewed in the context of the information provided in the report) in accordance with the standard?	<ul style="list-style-type: none"> • Does the report include enough information to help creditors understand the history of the company and the circumstances leading up to, and the need for, the appointment of a voluntary administrator? • Does the report include:

⁷ See Appendix 2 of this report for a summary of this guidance. The IPA is currently reviewing its published guidance to release as part of a comprehensive ‘Code of Professional Practice’. We based our review on the guidance applicable during the review period.

⁸ The standard consists of:

- current statutory requirements: see Appendix 1;
- the application of case law principles – but only to the extent that these principles set a standard that can be measured objectively; and
- mandatory guidance in the IPA Statement of Best Practice (i.e. the *shall* guidance as set out at Appendix 2)

Criteria	Key question	Key aspects of the standard ⁸
		<ul style="list-style-type: none"> –details of the company's existing shareholders and officers and details of registered charges? –a summary of the company's historical financial results with preliminary analysis and commentary? –the directors' explanation for the company's difficulties and the administrator's opinion on the reasons for the company's difficulties? –details of creditors who are related entities and the quantum of their claims? –a comment on whether or not the company has engaged in insolvent trading? –a comment on what investigations were done into voidable transactions including uncommercial loans, unfair preferences and unfair loans? –the estimated return to creditors from a winding up of the company? –the likely timing of the return to creditors from an immediate winding up of the company?
Quality of information in the report	Did the report adequately provide creditors with enough information to make an informed decision about the future of the company, in accordance with the standard?	<ul style="list-style-type: none"> • Are the key features of the DOCA disclosed? • Does the report include an estimated return to creditors under the DOCA? • Does the report include the administrator's reasoning about why the DOCA will provide creditors with a greater return than liquidation?
Opinions	Were the required three opinions expressed and reasons for those opinions provided?	<ul style="list-style-type: none"> • Does the report state the administrator's opinion on whether it would be in the creditors' interests for: <ul style="list-style-type: none"> –the company to execute a DOCA; –the administration to end; and –the company to be wound up? • Does the statement include soundly-based reasons for these opinions?

Disclosure of objectivity	Did the administrator comment on prior involvement with the company, its officers or related parties?	<ul style="list-style-type: none"> • Are there any issues raised in the report that should have been the subject of a separate disclosure to creditors by the administrator? • Note: Consistent with industry guidance, we reviewed whether this disclosure was made with the notice of the first report to creditors rather than the s439A report.
Remuneration	Did the administrator provide the required information in seeking remuneration approval?	<ul style="list-style-type: none"> • Does the report set out the basis and estimate of total remuneration sought for the administration, DOCA and liquidation periods?
Timeframe	Was the s439A report sent out within the timeframe required by s439A(5) of the Corporations Act?	<ul style="list-style-type: none"> • If the administration begins in December or less than 28 days before Good Friday, the meeting must be convened within 28 days. • Otherwise, the meeting must be convened with 21 days.

Moderation

After the assessments were completed, three assessors took on the additional role of moderators and set moderation parameters. To ensure consistency across reports, they assessed against the moderation parameters those aspects of a report where it was concluded that the administrator did not meet the standard. The findings in this report are the post-moderation results.

We are confident that the results from this review are accurate, fair and consistent and represent a reliable view of the quality of reporting to creditors by voluntary administrators on DOCA proposals during the selected period.

B Findings on the quality of investigations, reports and other requirements

Key points

Our review leads us to the overall conclusion that for the majority of reports, administrators either:

- did not undertake an adequate investigation, or
- did not fully report to creditors on the results of that investigation. Many reports failed to provide sufficient information about the company's business, property, affairs and financial circumstances to enable creditors to make an informed decision on whether accepting the DOCA proposal would be better than voting to place the company into liquidation.

We have reported our findings on the basis of the:

- quality of investigations;
- quality of reports to creditors; and
- other requirements (opinions; disclosure of objectivity; remuneration; timeframe; use of pro formas and clarity and presentation), based on the standard associated with the reporting process.

Quality of investigations

Investigating and reporting on the history of the company and the circumstances leading to the appointment

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✘ In general, administrators either did not investigate the history of the company or did not include the results of this investigation in the report. ✘ In 25% of reports, the administrator did not reveal the circumstances leading to, and the need for, their appointment.

Commentary on results

In general, the reports failed to meet those aspects of the standard that relate to inquiry and investigations into the history of the company. This indicates that the administrator either failed to undertake the necessary investigations or failed to fully report on these investigations.

Although most reports complied with the standard in containing constitutional information about the company, we identified cases where little or no information was provided about the circumstances leading up to,

and the need for, the appointment of a voluntary administrator. Reports often recorded the symptoms of failure (e.g. receipt of a demand for payment on a tax liability) rather than the causes of failure.

Although this information is historical, it is an administrator's obligation to investigate the affairs of the company and advise creditors of their findings. Relevant historical information is also useful for creditors to understand the context of the decision they face on the future of the company. This information is especially important where a DOCA is proposed that relies on future trading profits.

Offering preliminary analysis and commentary on the financial results

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✓ The company's historical financial results were included in 85% of reports. This requires the administrator to obtain and include in the report financial results prepared by the company. ✗ Preliminary analysis and commentary on the financial results were included in only 59% of reports. This is the more important requirement as it requires the administrator to consider the financial results and explain their significance to creditors.

Commentary on results

Preliminary analysis on the historical financial results was provided in only 59% of the reports reviewed. This information is important when creditors are considering whether to accept a DOCA that relies in full or in part on the future trading of the company as it provides information that may assist creditors assess the likelihood of the terms of the proposed DOCA being achieved.

Providing director's reasons for the company's difficulties and the administrator's opinion on these reasons

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✓ In 92% of reports an explanation provided by the directors for the company's difficulties was reproduced in the report. ✗ In 33% of the reports the administrator did not provide an opinion on these reasons. This means creditors were not given information about whether the directors' explanation was reasonable.

Commentary on results

When an administrator does not give an opinion on the reasons for the company's difficulties, particularly when the director had provided an

explanation for the company's difficulties, this suggests that the administrator either did not:

- investigate the reasons for the company's difficulties as indicated by the directors or
- report their findings to creditors.

Information about related party debts

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✓ In 90% of cases, the administrator identified related party creditors and the amounts owed to these creditors. ✗ We noted however that the legitimacy of most related party claims either were not considered or not discussed. Therefore, creditors were not informed about whether claims by related parties were real debts.

Commentary on results

If an administrator fails to analyse related party claims and establish whether the claims are legitimate or not, non-related party creditors can be disadvantaged because related parties without legitimate claims may:

- be allowed to vote on a DOCA proposal and may have sufficient voting strength to determine the result of the vote;
- alter dividend estimates in a comparison of DOCA and liquidation scenarios; and/or
- offer to 'forgive' their debt in a DOCA and therefore unduly affect other creditors' views on the relative attractiveness of the DOCA proposal compared to liquidation.

Information on the nature of the debt and how it was incurred is important in analysing the legitimacy of a claim by any creditor, but is particularly important for related parties.

Even where reports complied with the standard and commented on related entities and the quantum of their claim, in several cases it was difficult to identify this information as it was embedded in tables and not specifically addressed in the body of the report.

Given the potential for illegitimate related party debts to influence the outcome of the creditors' decision and disadvantage other creditors, it is important that administrators:

- not only verify the legitimacy of related party debt, but also
- report to creditors on this, including informing them of the amount of the debt, the nature of the debt and the circumstances giving rise to the debt.

Reporting on the likelihood of insolvent trading

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✘ Although most administrators commented on whether or not the company engaged in insolvent trading, only a minority (37%) gave an opinion on the likelihood of recoveries from successful litigation against one or more directors, or made an attempt to estimate the quantum of the likely or possible recoveries in the event of a successful recovery action. ✘ In the 235 reports where insolvent trading was identified, only in 38% was a date provided as to when the company may have been insolvent and only in 35 or 15% was there an estimate of the loss incurred.

Commentary on results

Although most administrators commented on whether or not the company engaged in insolvent trading, only a minority provided an opinion on the likelihood of recoveries from successful litigation against one or more directors, or attempted to estimate the quantum of the recoveries in the event of a successful recovery action. Although not mandatory under the industry guidance, without this information it is difficult to see how creditors could adequately compare the financial benefits of accepting a DOCA as opposed to voting to place the company into liquidation.

It is difficult to assess the likelihood of a successful litigation or any subsequent recovery from the personal assets of a director. However, we consider it is reasonable, where the administrator identifies the possibility that a company has engaged in insolvent trading, to support that opinion with information about the possible date of insolvency, an initial estimate of the loss incurred during the period of insolvency, and some preliminary analysis of the likelihood of recovery and the associated risks of recovery.

Where administrators did comment on the likelihood that the company had been trading while insolvent, the focus of reporting to creditors was more on the difficulties of proceeding with insolvent trading claims rather than setting out the disadvantages and advantages of all available options.

While we understand that it can be difficult, time consuming and costly to investigate insolvent trading, we consider that creditors need a more balanced view based on a preliminary investigation when making a decision on the future of the company.

If the administrator is of the opinion that it is inappropriate to make disclosure concerning the likely recovery from an insolvent trading action, the reasons should be disclosed in the report.

Reporting on voidable transactions

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✓ Most administrators commented on investigations conducted into potential preference recoveries. In 40% of reports the administrator estimated the likely returns from such actions. ✗ 28% of reports did not address unfair loans. <p>Voidable transaction recoveries are only available in a liquidation, not a DOCA.</p>

Commentary on results

For investigations into voidable transactions, most administrators commented on investigations they conducted into unfair preferences. However, it appears, based on our review, that in 28% of cases, unfair loans were not addressed. It is therefore unclear whether the administrator conducted investigations into unfair loans and whether or not funds may be available to creditors from this source if the company were placed into liquidation.

Books and records

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✓ 74% of reports incorporated an opinion as to whether the company's books and records were maintained in accordance with s286 of the Corporations Act.

Commentary on results

The administrator's opinion on the adequacy of books and records depends on the nature and size of the company. The administrator relies on their professional judgement in forming this opinion.

Adequate books and records are an important tool in monitoring a company's financial position and trading performance. They are necessary if the administrator is to conduct an adequate investigation into the company's business, property, affairs and financial circumstances and provide creditors with relevant information to enable them to make an informed decision about accepting the DOCA proposal or voting to place the company into liquidation.

Accordingly, whether adequate books and records have been kept, is relevant to creditors making an informed decision about the company's future.

Where the administrator suspects that they have not been provided with the books and records of the company this should be disclosed to creditors. In these circumstances, it is unlikely the administrator would be in a position to properly investigate the business, property and affairs of the company and therefore it would be difficult to recommend that creditors accept a DOCA proposal rather than vote to place the company into liquidation.

Estimated return in a winding up

Criteria	Main findings
Quality of investigation	<ul style="list-style-type: none"> ✓ Administrators provided an estimated return in the winding up in 95% of reports with 68% estimating a nil return. ✗ However, a large number reports did not include estimates of any return from potential insolvent trading or voidable transaction recoveries even though the possibility of such claims had been identified, and so the calculation of these estimates were incomplete.

Commentary on results

Our review did not consider whether estimates provided were accurate.

A large number of administrators failed to include estimates of any return from insolvent trading and voidable transactions when completing their calculations even though potential claims for either or both were identified.

In addition, we found that estimated returns failed to take into account administration and liquidation disbursements, which would dilute any estimated return.

We appreciate the difficulty in estimating returns, particularly given time constraints. However, we consider that high, low or best and worst case estimates should be provided so creditors have information on the likelihood and estimated quantum of potential returns for comparison and decision making purposes.

Quality of information in the report

Disclosure of the key features of the DOCA

Criteria	Main findings
Quality of information in the report	<ul style="list-style-type: none"> ✓ In 98% of cases the key features of the DOCA were disclosed. Details of the DOCA proposal are obtained from the DOCA proponents. ✗ When future trading was contemplated as part of a DOCA proposal, in 60% of these reports, the administrator failed to discuss how the company's trading prospects would be improved given the company's previous trading position. A DOCA based on future trading involves risk for the creditors and so creditors are placed at a significant disadvantage if they are not fully informed about future trading prospects. ✗ In 76% of reports there was no disclosure of the prospective financial information relied on for the DOCA proposal. ✗ In 78% of reports the administrator did not comment on the validity of the assumptions made in constructing the prospective financial information.

Commentary on results

We found that in 98% of cases the key features of the DOCA were disclosed. The key features were either found in summary format in the body of the report, or a copy of the draft DOCA was attached to the report or the proposal put forward by the director. It was not part of the review to check that the key features of the DOCA as disclosed to creditors prior to the vote were reflected accurately in the deed that was subsequently executed by the company and the deed administrator.

Estimated return under a DOCA and timing

Criteria	Main findings
Quality of information in the report	<ul style="list-style-type: none"> ✓ 95% of reports included an estimate of the return to creditors under the DOCA and 97% included some reasons from the administrator as to why the DOCA would provide creditors with a greater return than in liquidation. ✗ In 60% of reports the administrator failed to provide details of monitoring and reporting arrangements to be put in place to ensure the terms of the DOCA were satisfied. A lack of monitoring of the DOCA increases the risk that creditors may not receive the promised returns under the DOCA. ✗ In 81% of reports the administrator failed to include details of how creditors were to be informed of the progress of the DOCA.

Commentary on results

In 60% of reports the administrator failed to provide details of monitoring and reporting arrangements to be put in place to ensure the terms of the DOCA were satisfied.

Some proposed DOCAs provide for a dividend to be paid only following the performance of specified events at some time in the future. In these circumstances, when creditors are deciding whether to accept the proposed DOCA or vote to place the company into liquidation, they would benefit from information on:

- how compliance with the terms of the proposed DOCA will be monitored, and
- progress.

Trading during the DOCA period

Criteria	Main findings
Quality of information in the report	<p>Insufficient information about future trading</p> <ul style="list-style-type: none"> ✗ Where future trading was contemplated as part of the DOCA proposal, the majority (60%) of reports did not contain any explanation as to the changes

Criteria	Main findings
	<p>that would be made to ensure the future trading would be more financially successful than previous trading.</p> <ul style="list-style-type: none"> ✘ Also relevant is the lack of disclosure (reported above) on both prospective financial information and the underlying assumptions.

Commentary on results

Where future trading was considered as part of a DOCA proposal, the majority of reports failed to:

- disclose how the company's trading prospects would be improved when compared to the company's previous trading position; and/or
- include a summary of the prospective financial information relied on in proposing the DOCA and did not include the assumptions relied on in the financial information.

In these circumstances creditors would be likely to favour a DOCA as the estimated return is greater than liquidation, even though the basis for the DOCA return has not been adequately assessed and in some cases was based on assumptions and projections that did not appear to be attainable.

Other requirements

As part of our review of the quality of reports under s439A we assessed a range of other requirements based on the standard associated with the reporting process.

Inclusion of the three required opinions

Main findings
<ul style="list-style-type: none"> ✘ The law requires the expression of three opinions by the administrator in the reports. Sometimes, the expression of a strong opinion in favour of the DOCA proposal means that creditors can infer that the other two options are not favoured. An administrator is required to disclose the opinions anyway. This did not occur in all reports reviewed. ✓ However, for the purpose of the review we accepted that in 94% of cases at least one opinion was expressed and it would have been clear to creditors which option the administrator was recommending and why.

Commentary on results

Although we have classified 94% of reports as meeting the standard in this area, we note that separate and clear reasons for the administrator's opinion about each option were not always provided in the reports, even though this is

expressly required by s439A, confirmed in case law, and reiterated as a compulsory requirement in the IPA Statement of Best Practice. Where creditors could have inferred from the reason(s) provided for at least one option what the reason for not recommending the alternative options was, we treated the report as meeting the standard.

Disclosure of objectivity

Main findings

- ✓ 94% of reports included a comment by the administrators about their earlier involvement with the company, its officers or related parties, either by including a statement to the effect that there was no earlier involvement or describing an earlier involvement.
- ✓ In 31% of reports, the administrators advised that they had an earlier involvement with a related party. Of those, 80% disclosed the identity of the related party, 73% disclosed the nature and extent of related party involvement and 64% disclosed the period of time over which the earlier involvement persisted.
- ✗ Some relationships that should have been disclosed were not disclosed.

Commentary on results

During the review, it became apparent that, in some cases, earlier relationships between the administrator and a related party (usually a director) were not disclosed. In some instances, the administrator had previously been administrator or liquidator of another company controlled by the current director. In such circumstances the administrator must carefully consider their independence to act and make full disclosure to creditors.

Administrators sometimes made a positive statement of independence but did not include any detail on any relationships reviewed as part of the analysis of independence. Administrators are required by law to be, and be seen to be, independent. Where this legal obligation is not met as a question of fact, disclosure cannot cure a breach. For example, in one report, an administrator advised that he had previously been the liquidator of a company, sold its business and was now administrator of the purchaser company.

Remuneration disclosures

Main findings

Disclosure of the quantum of remuneration

- ✓ In most reports, the quantum of remuneration was disclosed (voluntary administration 92%, DOCA 93% and liquidation 90%).
- ✗ In some reports, details of the quantum of remuneration being claimed was not separately noted in the body of the report, but was included on a proxy form, as part of a dividend estimate, on a notice of meeting or in the first circular to

Main findings

creditors.

Disclosure of sufficient information to allow creditors to assess the reasonableness of remuneration

- ✘ Many reports did not contain any information on the work performed or to be performed to justify the quantum of remuneration claimed (voluntary administration 39%, DOCA 67% and liquidation 68%).

Commentary on results

Provision of information only on the quantum of remuneration claimed does not give creditors sufficient information to assess reasonableness.

Creditors are being asked to approve remuneration but are not having their attention drawn to the justification for that remuneration when:

- information about remuneration is not explained adequately in the report and
- the quantum of remuneration being claimed is not separately noted in the body of the report, but contained on a proxy form, in a dividend estimate, on a notice of meeting or in the first circular to creditors.

Within the statutory timeframe

Main findings

- ✓ Of the 275 reports reviewed, 271 (99%) were sent out within the specified time period.
- ✘ Four reports were sent out a day late (based on the date of the report).
- ✓ In 19% of reports, the administrator recommended an extension of the time period.
- ✓ In 5% of cases, the administrator had sought an extension of the convening period.

Commentary on results

Several administrators advised that they were unable to investigate certain matters further due to time constraints and information not provided to them at the date of the report. These administrators did not seek an extension of the convening period or recommend an adjournment of the second meeting of creditors to investigate matters further and to obtain the company's records or if the meeting was adjourned they did not conduct further investigations into matters.

This means that their recommendations to creditors were based on incomplete investigations and information.

Use of proforma reports

Main findings

- ✘ Many administrators use a standard template for reporting and a small minority do not tailor the template. This resulted in bulky and unnecessary information being provided in the report that was irrelevant to the decision to be made by creditors concerning the company's future.

Clarity and presentation

- ✘ Some reports were poorly organised so that creditors may have difficulty identifying information relevant to making a decision about the company's future.

Commentary on results

We note that most firms/administrators use a standard template in completing their s439A reports. Such templates are used as a formatting tool and a guide for including all matters that are to be addressed in the report.

Although most reports were tailored to account for the issues relevant to the company, up to 25% of reports were not adequately tailored. These reports maintained a standard form and included information that was not relevant and did not add value to the report.

Other problems with these proforma reports included:

- voluminous information explaining voidable transactions and insolvent trading without detailing how this information is relevant to the company or tailoring that information to the company;
- a standard description of tasks undertaken during the voluntary administration process that included tasks that were not relevant to a particular administration (e.g. one report referred to dealing with suppliers and approving purchase orders during an administration where no business was being traded);
- a large amount of information documenting and describing the administration process that in reality added no value to the s439A report and would have been more appropriately included in the first circular to creditors; and
- standard paragraphs when commenting on assets and liabilities that are not relevant to the company.

C Recommendations for future action

For a list of our major recommendations for improvements to reports, refer to the table in the executive summary.

Creditors rely on the competence, independence and professionalism of voluntary administrators in presenting them with information and advice so they can make a fully informed decision on the future of a company in which they are financially involved.

We have reviewed a large sample of reports presented by administrators in real-life situations and compared the quality of some aspects of those reports with a standard.

We have identified a range of issues and suggested areas for improvement.

Through our compliance role, and through our continuing liaison with the IPA and the corporate insolvency industry, we will be working towards:

- improving industry guidance so that it promotes administrators' reports meeting the requirements of the guiding rule of providing creditors with sufficient information to enable them to make an informed decision about the options available to a company under administration;
- making administrators aware of their legal obligations; and
- raising the standard of reporting to creditors.

The *Corporations Amendment (Insolvency) Act 2007* and the *Corporations Amendment Regulations 2007* have introduced some measures that clarify the obligations of administrators including:

- an additional requirement in s439A(4) for administrators to set out such other information known to the administrator as will enable creditors to make an informed decision about each of the matters covered in the report;
- additional requirements for disclosure to creditors prior to seeking remuneration approval;
- recording of reasons for the decision to exercise or not exercise a casting vote at a 439A meeting;
- extensions of the time periods for holding meetings in a voluntary administration; and
- provision to creditors of declarations of relevant relationships and indemnities at the first meeting of creditors.

We are:

- bringing the contents of this report to the attention of practitioners so they, and the IPA, can address the findings through improvement of their practices and guidance;

- paying particular attention to s439A reports as part of our ongoing compliance work; and
- intending to conduct a further review at a future time to assess whether there has been an increased standard of compliance, particularly given the amended statutory provisions.

We recommend that:

- practitioners have regard to the reported findings of our review and address any shortcomings in their own practices; and
- creditors ask the administrator questions where they are in any doubt about the information being presented to them.

In future cases, we will consider all available options where we are of the view that creditors have not been provided with the requisite information to support their decision-making. Following recent insolvency law reform we now have standing as an applicant under s445D of the Corporations Act to seek to have a DOCA terminated by the court in certain circumstances.

Appendix 1: Statutory requirements for s439A reports⁹

Obligation to investigate

Section 438A specifies:

As soon as practicable after the administration of a company begins, the administrator must:

- (a) investigate the company's business, property, affairs and financial circumstances; and
- (b) form an opinion about each of the following matters:
 - (i) whether it would be in the interests of the company's creditors for the company to execute a deed of company arrangement;
 - (ii) whether it would be in the creditors' interests for the administration to end;
 - (iii) whether it would be in the creditors' interests for the company to be wound up.

In carrying out this investigation, the administrator is assisted by a statutorily imposed duty on the directors to help the administrator (s438B) and the administrator's right to the company's books: s438C.

The administrator must also report to ASIC any wrongdoing discovered during the investigation: s438D.

Obligation to report to creditors

When calling the meeting of creditors to decide the company's future, the notice of meeting must be accompanied by a copy of:

- (a) a report by the administrator about the company's business, property, affairs and financial circumstances; and
- (b) a statement setting out the administrator's opinion (and his or her reasons for those opinions) about each of the following matters:
 - (i) whether it would be in the creditors' interests for the company to execute a deed of company arrangement;
 - (ii) whether it would be in the creditors' interests for the administration to end;

⁹ These statutory requirements are presented as they stood at the time of our review and prior to the amendments introduced through the *Corporations Amendment (Insolvency) Act 2007* and *Corporations Amendment Regulations 2007*.

- (iii) whether it would be in the creditors' interests for the company to be wound up; and
- (c) if a deed of company arrangement is proposed—a statement setting out details of the proposed deed.

In setting out the opinions in the statement mentioned in s439A(4)(b), the administrator must specify whether there are any transactions that appear to the administrator to be voidable transactions in respect of which money, property or other benefits may be recoverable by a liquidator under Pt 5.7B: reg 5.3A.02.

The voidable transactions covered in Division 2 of Pt 5.7B are unfair preferences (s588FA), uncommercial transactions (s588FB), insolvent transactions (s588FC), unfair loans to a company (s588FD), unreasonable director-related transactions (s588FDA) and related entity benefits from an insolvent transaction (s588FH).

Matters that the creditors must decide

At the meeting to decide the company's future, creditors *may* resolve that:

- (d) the company execute a deed of company arrangement specified in the resolution (even if it differs from the proposed deed (if any) details which accompanied the notice of meeting); or
- (e) the administration should end; or
- (f) the company be wound up.

These are three mutually exclusive alternatives.

Appendix 2: IPA Statement of Best Practice—Content of an Administrator’s Report

	‘Shall’	‘Should’	‘May’
7.1 Background Information	The administrator’s report <i>shall</i> contain sufficient information to provide creditors with an understanding of the history of the company and the circumstances leading up to and the need for the appointment of a voluntary administrator.		
<i>7.1.1 Shareholders and Officers</i>	The administrator’s report <i>shall</i> incorporate details of the company’s existing shareholders and officers and details of registered charges.	Changes in these details that have occurred within twelve months before the administrator’s appointment <i>should</i> also be disclosed.	
<i>7.1.2 Books and records</i>		The administrator’s report <i>should</i> incorporate an opinion as to whether the company’s books and records are maintained in accordance with s286 of the Corporations Act.	
<i>7.1.3 Financial statements</i>		The administrator’s report <i>should</i> disclose the date to which the company’s financial statements were prepared prior to the administrator’s appointment.	
<i>7.1.4 Historical financial performance</i>	The administrator’s report <i>shall</i> incorporate a summary of the company’s historical financial results and a preliminary analysis and commentary thereon.		
7.2 Administrator’s prior involvement		Whilst it is acknowledged that the administrator should detail his prior involvement with the company at the first meeting of creditors, the administrator’s report <i>should</i> reiterate those circumstances and disclose any prior involvement with the company, its officers or any related parties.	

	'Shall'	'Should'	'May'
7.3 Current financial position of the company			
7.3.1 <i>Directors' report as to affairs</i>		The administrator's report <i>should</i> outline the content of the directors' report as to affairs and include the administrator's comments as to the administrator's estimate of realisable value of assets and liabilities.	
7.3.2 <i>Explanations for difficulties</i>	The administrator's report <i>shall</i> include the directors' explanation for the company's difficulties and the administrator's opinion on the reasons for the company's difficulties.		
7.3.3 <i>Outstanding winding-up applications</i>		The administrator's report <i>should</i> disclose any winding up applications filed against the company prior to the appointment of the administrator and the petitioning creditor in such applications.	
7.3.4 <i>Related entities</i>	The administrator's report <i>shall</i> disclose those creditors of the company who are related entities and the quantum of their claims.		
7.4 Offences, voidable transactions and insolvent trading			The administrator <i>may</i> disclose suspected offences in the administrator's report, where they appear materially relevant to the creditors' decision on the company's future.
	The administrator's report <i>shall</i> include comment regarding whether the company engaged in insolvent trading.	The administrator <i>should</i> disclose the quantum of any voidable transactions identified during the investigation and <i>may</i> disclose the beneficiaries of those transactions.	The administrator's report <i>may</i> provide an estimate of the loss incurred by the company as a result of insolvent trading.
		The administrator's report <i>should</i> disclose a director's personal financial position where the director intends to maintain an interest in the company after the proposed deed	

	'Shall'	'Should'	'May'
		is executed, if the director may be liable to compensate the company as a result of an antecedent transaction or insolvent trading in a winding up. When a director does not provide this information, or authorise its disclosure by third parties, this should be disclosed in the report.	
7.5 Estimated return from a winding up	<p>The administrator's report <i>shall</i> disclose:</p> <ul style="list-style-type: none"> • the estimated return to creditors from a winding up of the company; and • the likely timing of the return to creditors from a winding up of the company; and • the basis on which remuneration will be sought by the liquidator including an estimate of the likely costs of administering the winding up of the company. 		
7.6 Proposal for a deed of company arrangement		<p>Where a DOCA is being proposed, the administrator's report <i>should</i> disclose:</p> <ul style="list-style-type: none"> • the key features of the proposed DOCA (s439A(4)(c)); • the estimated return to creditors and likely timing of the return to creditors from the proposed DOCA; • the monitoring and reporting arrangements that are to be put in place to ensure that the terms of the DOCA are met and that creditors are fully informed of the progress of the administration; • a summary of the administrator's reasoning as to why the DOCA will provide creditors with a greater return than in a liquidation, and if future trading under the DOCA is contemplated, how the intended 	

	'Shall'	'Should'	'May'
		<p>trading will enhance the return to creditors given the trading position of the company prior to the administrator's involvement;</p> <ul style="list-style-type: none"> • subject to commercial confidentiality, a summary of the prospective financial information relied upon for the proposed DOCA and the assumptions relied upon in the preparation of the prospective financial information; • subject to commercial confidentiality, a comment on the validity of the assumptions relied upon in preparing the prospective financial information, if the prospective financial information was prepared by a third party. If the prospective financial information was prepared by the administrator, the administrator should summarise the key assumptions relied upon in preparing the prospective financial information; • in circumstances where a guarantor proposes to retain control of the business under the proposed DOCA, details of the creditors holding the guarantees and the quantum of the debt secured by the guarantees. The report should request that any creditor holding a guarantee which is not disclosed in the report provide details to the administrator as soon as possible. 	
7.7 Administrator's Opinion	The administrator <i>shall</i> express an opinion and reasons for the opinion, as to whether the option is in the creditors' interests, in regard to each of the options available to the creditors to decide pursuant to s439C of the Corporations Act.	The administrator <i>should</i> advise creditors in writing, if practicable, of any additional matter that comes to the administrator's attention after the dispatch of the administrator's report that a reasonable person would consider to be material to the creditors' decision.	

	'Shall'	'Should'	'May'
8 Other Material Information	The administrator's report <i>shall</i> include any other information that is materially relevant to the creditors' decision on the company's future.		
Remuneration	<p>The administrator's report <i>shall</i> disclose:</p> <ul style="list-style-type: none"> the basis on which remuneration will be sought by the administrator and an estimate of total remuneration sought by the administrator; the basis on which remuneration will be sought by the administrator of the proposed DOCA and an estimate of the total remuneration payable for administering the proposed DOCA. 		

Key terms

Term	Meaning in this document
Corporations Act	<i>Corporations Act 2001</i>
deed administrator	An independent person, who must be a 'registered liquidator', who performs certain duties and exercises certain powers in a DOCA in accordance with Part 5,3A of the Corporations Act and the terms of the deed
DOCA	Deed of company arrangement, which follows from a voluntary administration where creditors accept a proposal for continuation of a company or its business on certain conditions
Guiding rule	The requirement based on statute and case law for an administrator to provide sufficient information to creditors to enable the creditors to make an informed decision on the three options presented in a voluntary administration.
IPA Statement of Best Practice	Insolvency Practitioners Association, 'Statement of Best Practice—Content of an Administrator's Report Pursuant to Section 439A(4) of the Corporations Law' (sic) effective 1 July 2001
LCU	ASIC's Liquidator Compliance Unit, which co-ordinated the review
registered liquidator	An insolvency practitioner registered under Part 9.2 of the Corporations Act who is entitled to be appointed to particular roles specified in Chapter 5 of that Act
the standard	Consists of: <ul style="list-style-type: none"> • current statutory requirements; • the application of case law principles – but only to the extent that these principles set a standard that can be measured objectively; and • mandatory guidance in the IPA Statement of Best Practice (i.e. the <i>shall</i> guidance)
s439A report	A report prepared by an administrator to creditors about the company's business, property, affairs and financial circumstances as well as the liquidator's opinion on the options available for the future of the company, the administrator's reasons for those opinions and details of any proposed DOCA
voluntary administration	A formal insolvency appointment aimed at rehabilitation of a company or its business or producing a higher return to creditors than liquidation. Refer Part 5.3A of the Corporations Act

Term	Meaning in this document
voluntary administrator	An independent person, who must be a 'registered liquidator' who performs certain duties and exercises certain powers in a voluntary administration in accordance with Part 5.3A of the Corporations Act

Related information

Legislation

Pt 5.3A *Corporations Act 2001*

Other related guidance and papers

Insolvency Practitioners Association, Statement of Best Practice—Content of an Administrator’s Report Pursuant to Section 439A(4) of the Corporations Law’ (sic) effective 1 July 2001