



# Disaster Recovery Fact Sheet

## Directors' liabilities where likely to be trading insolvent

▼ CHAMBER OF COMMERCE AND INDUSTRY QUEENSLAND FACT SHEET

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## **DIRECTORS' LIABILITIES WHERE LIKELY TO BE TRADING INSOLVENT**

Chamber of Commerce and Industry Queensland is aware that the current situation with the flooding and cyclones in Queensland may lead to some companies trading insolvent. This fact sheet provides an overview of some of the Director's duties and liabilities with regards to insolvent trading and provides an overview of the options companies have and the possible penalties and consequences if they trade when insolvent.

### **DIRECTORS' DUTIES**

If your company is insolvent, or there is a real risk of insolvency, your duties expand to include creditors (including employees with outstanding entitlements).

### **DUTY TO NOT TRADE WHILE INSOLVENT**

As well as general Director duties, you also have a positive duty to prevent your company trading if it is insolvent. A company is insolvent if it is unable to pay all its debts when they fall due. This means that before you incur a new debt, you must consider whether you have reasonable grounds to suspect that the company is insolvent or will become insolvent as a result of incurring the debt.

An understanding of the financial position of your company only at the time you sign off on the yearly financial statements is insufficient. You need to be constantly aware of your company's financial position.

### **DUTY TO KEEP BOOKS AND RECORDS**

For the purposes of an insolvent trading action against a Director, a company will generally be presumed to have been insolvent throughout a period where it can be shown to have failed to keep adequate financial records.

### **WHAT TO DO IF YOUR COMPANY IS INSOLVENT**

If your company is insolvent, do not allow it to incur further debt. Unless it is possible to promptly restructure, refinance or obtain equity funding to recapitalise the company, generally your options are to appoint a voluntary administrator or a liquidator. So first determine whether it is possible for you to make such arrangements with your bank, lender, suppliers and creditors generally that will assist in keeping you viable and solvent over the period of recovery. If not, and you believe you are and will be trading insolvent then you have the following options.

### **VOLUNTARY ADMINISTRATION**

This can be defined when an independent and suitably qualified person (the voluntary administrator) is appointed and takes full control of the company to try to work out a way to save either the company or the company's business. If it isn't possible to be saved, the aim

is to administer the affairs of the company in a way that results in a better return to creditors than they would have received if the company had instead been placed straight into liquidation. Putting a company into voluntary administration can be done by the board of the company resolving that the company is insolvent, or likely to become insolvent. The Director also needs to obtain the written consent of a registered liquidator to act as voluntary administrator.

## **LIQUIDATION**

The purpose of liquidation of an insolvent company is to have an independent and suitably qualified person (the liquidator) take control of the company so that its affairs can be wound up in an orderly and fair way for the benefit of its creditors. Generally, a Director-initiated liquidation involves calling a meeting of members to vote on winding up the company and the appointment of a liquidator or applying to Court to wind up the company.

## **RECEIVERSHIP**

A company most commonly goes into receivership when a receiver is appointed by a secured creditor who holds security over some or all of the company's assets. The receiver's primary role is to collect and sell sufficient company charged assets to repay the debt owed to the secured creditor.

## **PENALTIES AND CONSEQUENCES OF INSOLVENT TRADING**

There are various penalties and consequences of insolvent trading, including civil penalties, compensation proceedings and criminal charges.

### **CIVIL PENALTIES**

Contravening the insolvent trading provisions of the Corporations Act can result in civil penalties against Directors, including pecuniary penalties of up to \$200,000.

### **COMPENSATION PROCEEDINGS**

Amounts lost by creditors can be initiated by ASIC, a liquidator or a creditor against a Director personally and a compensation order can be made in addition to civil penalties.

Compensation payments are potentially unlimited and could lead to the personal bankruptcy which disqualifies that Director from continuing as a Director or managing a company.

### **CRIMINAL CHARGES**

If dishonesty is found to be a factor in insolvent trading, a Director may also be subject to criminal charges (which can lead to a fine of up to \$220,000 or imprisonment for up to five years, or both). Being found guilty of the criminal offence of insolvent trading will also lead to a Director's disqualification.

To ensure adequate protection, please contact CCIQ Law to discuss on 1300 405 711.