

Claims Against Directors During a Liquidation

Many directors think (wrongly) that once a company enters liquidation, it is no longer their “problem”. Quite the contrary, although the liquidator takes control of the company, and quite apart from obligations of a director to provide information and assistance to a liquidator, liquidation can be the catalyst for claims to be made against directors, exposing their personal assets to risk (amongst other things).

In fact, some claims against directors only exist *if* the company is in liquidation.

Claims which might be made against directors include (but are not limited to):

1. By a liquidator:

- a. Insolvent Trading Claims. These are claims by a liquidator against directors for amounts equal to debts incurred by a company (and unpaid) whilst it was insolvent.
- b. Uncommercial Transaction Claims. These are claims by a liquidator in respect of company transactions that a reasonable person in the company’s circumstances would not have entered into.
- c. Unfair Preference Claims. These are claims by a liquidator to recover amounts paid by the company to its creditors (a director can also be a creditor) within certain time periods prior to liquidation, and which have the effect of providing that creditor with a payment greater than they would have received had the company been liquidated and the creditor received a dividend in the liquidation.
- d. Director Loan Account Claims. These are simply claims by the company for recovery of debts owed by the director to the company.
- e. Breach of Directors Duties. Directors owe many duties to the company, and a company (by its liquidator) may bring claims against the director for breaches of any of those duties.

2. By creditors:

- a. Director Penalty Notice liability (ATO). Directors can be personally liable for a company’s PAYG and Superannuation liabilities, and as from 1 April 2020 for GST liabilities, either as a result of non-lodgment (automatic liability) or non-payment (21-day notice liability).
- b. Indemnity Proceedings / Unfair Preference (ATO). If unfair preference proceedings are brought by a liquidator against the ATO to recover amounts paid to the ATO within 6 months of the liquidation, the ATO can in turn claim some (or all) of those payments from the director.



- c. Personal Guarantees. Once the company is liquidated, company creditors who also hold a personal guarantee or indemnity from the director will likely look to the director for payment of the debt.
- d. It should also be noted that a liquidator has the power to conduct a Public Examination of directors. This is a process whereby a liquidator can apply to Court to summons a director to attend Court and give evidence on oath as to the affairs of the company. It is commonly used as a tool to determine whether there exists evidence, and to gather such evidence, for a claim by the liquidator against the director.

The above is not an exhaustive list. Nor does it explain the elements of the claims in detail or any defences that may be available to such claims. It is intended to illustrate only that liquidation does not resolve the personal exposure of directors in respect of a company's collapse.

With timely advice, the company's business may be able to be resurrected and liquidation might be able to be avoided by way of, amongst other things:

1. Business turnaround strategies;
2. Negotiations with key creditors and stakeholders;
3. Finance or re-finance; and/or
4. Re-structuring (formal or informal).

Accordingly, noting that liquidators will act in the best interests of company creditors, it is prudent **for directors** to seek advice as early as possible, including:

5. Before a company is liquidated (eg when there is pressure from the ATO or financiers or other creditors); and
6. After a company is liquidated.

Our Business Advisory, Turnaround and Insolvency team has saved many businesses from liquidation, provided creditors with a better return than liquidation, protected the assets of many directors, and assisted directors to defend actions by liquidators and guarantee creditors. We are pleased to offer a no obligation initial consultation (up to one hour) to explore your options.

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