# COVID-19 and Corporate Insolvency: What does an increase in corporate insolvency mean to creditors?

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In these difficult times, recent legislative amendments provide assistance for debtors, but risk for creditors. Going forward, it will be important for creditors to carefully monitor their credit policies. Creditors are likely see more spikes in default rates over the next months while government restrictions and businesses' staff isolation plans remain in place. Where a debtor is placed into external administration, they should be aware of their rights (and duties) during the insolvency process.

Creditors should take note of the changes to the bankruptcy and insolvency regimes designed to protect debtors during the coronavirus period. The changes will limit options to creditors in respect of certain enforcement action. They include:

1. An increase in the threshold for issuing statutory demands from $2,000 to $20,000;
2. An increase in the threshold for issuing bankruptcy notices from $5,000 to $20,000;
3. An increase in the period for a debtor's compliance with a statutory demand or

bankruptcy notice from 21 days to 6 months.

This means a recalcitrant debtor can hold off a creditor trying to collect money for at least 6 months. But the worst scenario for a creditor is finding out they are an unsecured creditor for a large sum owing by a company in external administration with no assets. Creditors should consider the options available to avoid becoming an unsecured creditor in a company's liquidation. Those include:

1. Limiting the amount of credit being offered to the debtor;
2. Restricting the period in which invoices must be paid;
3. Taking sufficient security from the debtor;
4. Ensure any PPSR charges have been appropriately registered over the company's assets;
5. Providing goods as cash on delivery;
6. Requiring prepayment for goods and services;
7. If the debtor is placed into voluntary administration, voting on or proposing a DOCA (for reasons discussed further below).

If creditors wish to take security, they should act swiftly to do so. Creditors may not be able to enforce their security taken in respect of existing debts if the debtor granted the security within 6 months prior to the external administration.

Where a debtor grants security while being subject to a winding up application there is a risk that the security becomes void. Accordingly, creditors should review relevant company searches and ensure that the debtor is not the subject of an action to wind up the company at the time of taking security from the debtor.

Where a debtor appoints a voluntary administrator ("**VA**"), creditors generally cannot enforce or take legal action as a result of the moratorium. This includes a lender wishing to take possession of property the subject of a mortgage or charge, as well as a landlord repossessing property under a lease. If there is a specific need to enforce a debt, a creditor may apply to a court to seek the court's permission to proceed with enforcement action. However, to convince a court they will require good reasons. They may also be faced with some difficulty given the current restrictions on physical access to courts.

Creditors should pay close attention to any Deed of Company Arrangement ("**DOCA**") proposal put forward, and may wish to consider putting forward their own in appropriate circumstances. If creditors do not vote in favour of a DOCA and the company is put into liquidation, the liquidator will review lump sum payments made to creditors within the 6 months prior to the VA's appointment and may be able to recover those sums from creditors as unfair preferences. It can therefore be of particular benefit to creditors who received any substantial repayment of their debt prior to the VA's appointment to vote in favour of a DOCA in order avoid a liquidator chasing them for preference payments.

Conversely, creditors should also pay attention to whether other creditors have received any preferential treatment in the repayment of their debts prior to the appointment of a VA. In that

case, they will need to weigh up any possible or expected recovery action that could be taken by a liquidator versus the expected outcome through the proposed DOCA.

Finally, the Australian Government has passed legislation whereby the Government will guarantee loans made by financial institutions (banks and non-ADI lenders) made to SMEs. Under the new legislation, the *Guarantee of Lending to Small and Medium Enterprises (Coronavirus Economic Response Package) Act 2020*, both existing and new loans can be considered. However, to qualify for the guarantee the Minister must be satisfied that the loan is likely to assist in dealing with the economic impacts of COVID-19. Up to $20 million may be appropriated. Lending entities should pay attention to further details of how this scheme operates and how they may utilise the scheme.

If you would like more information or advice in relation to insolvency, restructuring or debt recovery law, contact Andrew Hack at andrewh@matthewsfolbigg.com.au or a Principal of the Matthews Folbigg Insolvency, Restructuring & Debt Recovery Group:

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