

News with Clout

Providing Corporate & Personal Solvency Solutions

UNFAIR PREFERENCES UNCOVERED STEP 1

We often get asked in this region for help with strategies in which to thwart insolvency practitioners from clawing back your or your clients' hard earned income.

We will focus primarily on Corporations legislation and just highlight the various differences under bankruptcy legislation. Section 588FA of the Corporations Act calls them Unfair Preferences. The key ingredients of a clear preference are discussed following and brief ideas as to how to circumvent the issue.

The ability to claw back a Preference in the company context is only available to a liquidator. There also has to have been a debtor creditor relationship between the company in liquidation and the recipient of the funds. If you get paid by a third party where is the preference?

The transaction or transactions (if the running account issues apply) must have taken place within 6 months of the relevant date. The relevant date varies slightly but as a rule it is from the commencement of the winding up. Prior to that time there is no preference. Running account involves looking at all the transactions as they have occurred like in a statement or a ledger account and whether or not there was actually a reduction in the amount due over time. So you just do not look at the payment side of things. The invoices need to be included in the calculation as well. Do the calculations there may not actually have been a reduction in the last six months of the amount due.

The company in liquidation must have been insolvent at the time of or as a consequence of the transaction. So if the books and records or the company are adequate (as if they are not there is a presumption of insolvency) the liquidator needs to prove when the company

became insolvent and that it was insolvent for all time after that point. Ask the question. You will get access to an insolvency report once litigation has commenced so ask for it up front. If they are not hiding anything you will get to see it otherwise they have not yet done the work properly or are hiding something.

The transaction must have given the recipient of the funds an advantage over other creditors at the time of the transaction. This means that if the company had been wound up at the time of the transaction had the recipient actually received more than would have been received had the company been wound up at that time. If that is not the case then it is difficult for a liquidator to argue that the recipient had been preferred.

There are a couple of defenses in the Corporations Act that make it necessary that the liquidator needs to prove that the recipient did not receive the money in good faith and persuade the court that they had to have suspected that the company was insolvent. This is quite a task but made easier by correspondence emails round dollar amounts paid rather than specific invoices and the obvious withdrawal of credit when the ledger account is reconstructed. The message here is stay on them via phone, if there is to be partial payments make it for the older invoices and a specific amount. If in doubt always take the money as the mechanics of litigation ensures you take the money then fight the action.

In step 2 we consider various practical aspects of litigation in the context of an insolvency touch on how you can get certain information and how the background facts will determine if the liquidator will go to court or not.

As ever we welcome all your queries in and around financial distress.