

NICOLS + BRIEN INFORMATION SHEET L

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PERSONAL INSOLVENCY INFOPAK

PRACTICAL CONSIDERATIONS FOR THE DEBTOR

FACTORS TO CONSIDER WHEN CHOOSING THE MOST APPROPRIATE ADMINISTRATION FOR YOUR NEEDS

PART X OR BANKRUPTCY

The major factors when considering what type of administration are:

- ***Is a Part X a relevant consideration or is the individual in question just as well off going bankrupt. There must be some benefit to the debtor or there is no point in proceeding with a Part X:***
- ***Is the debtor able to provide a benefit to his creditors over and above what they might receive in bankruptcy.***

In dealing with the first issue, if the debtor can derive no tangible benefit or "upside" for themselves through entering into a Part X Arrangement then as long as they can live with the various bankruptcy conditions there is, in practical terms, no other alternative.

To properly consider this "first choice" you should have a firm understanding of the implications of bankruptcy and particularly how they relate to your desired future position.

A Part X Arrangement can be extremely beneficial to a debtor where there is some upside to their future financial position. This may be to protect potential Super profits from income to be derived or possibly to limit access by creditors to a particular asset, for example the family home. Other particular determinants may be:

- Continuity as an officer of the company without having to resort to applications to the Courts for approval to continue as a director.(subject to type and timing of part X entered into)
- Protection of particular assets such as the family home, an interest in a business, either company, partnership or a Trust.

- The debtor may be in a position to substantially increase the quantum of his income. They may be either prevented from participating in circumstances where they are a bankrupt.
- The debtor may wish to continue in business (which is difficult, but not impossible, in bankruptcy).
- There may be certain assets or rights, for example an interest in a Will, which do not presently vest in the debtor but may well vest in them in a time frame within which they might still remain an undischarged bankrupt.

Obviously these considerations form part of the "factors" that one should consider when choosing the type of administration ie, bankruptcy or Part X which best suits your needs. They are not conclusive, other factors may be relevant to the debtor's position.

PART X PRIMARY SUCCESS FACTORS

- *There must be a benefit to the creditors over and above what they might receive in a bankruptcy scenario.* (Even if this benefit is merely one of crystallising to certainty, for example income contributions. In bankruptcy, they might be available subject to the future income prospects of the bankrupt. Under a Part X scenario, the income contributions can be quantified thereby providing creditors with some certainty, as opposed to doubt and unpredictability).
- *There must be a benefit to be derived by the debtor.* (The mere statement that the debtor avoids bankruptcy is not sufficient. There should be a tangible benefit to the debtor).
- *The terms of the Part X proposal must be realistic.* (They must be something that is achievable by the debtor).

FACTORS FOR CONSIDERATION

The following points are not specific to the success or otherwise of the Part X but are practical points to keep in mind when both considering and/or formulating an offer to creditors under a Part X:

- The best offer is one which provides for immediate payment to creditors. The time value of money is a relevant consideration.
- A bench mark as to the potential dividends in bankruptcy should be set. This will set a target which should be bettered if the offer is to appear reasonable.

- Are there any transactions entered into by the debtor which might fall foul of the various claw back provisions of the Bankruptcy Act? For example undervalued transactions, transfer to defeat creditors or preferences within either two or five years (Section 120 to 122 of the Bankrupt Act). These aspects will have some bearing on funds available in bankruptcy and therefore need consideration.

- Assets the debtor wishes to preserve.

Is the debtor's spouse also bound by guarantees relating to the same indebtedness? Consider either a joint administration or an administration where the spouse is not required to effectively do anything but obtain release from creditors claims with the primary benefits to creditors coming from the Part X of the debtor.

- Who are the creditors of the debtor? This can be of particular relevance given the voting requirements for a meeting under a Part X.

Given voting rights at the meeting it is appropriate to attempt to determine the attitude of the primary creditor, if relevant, prior to a Part X proposal being put forward.

- Are there debts due to associated creditors? Associated in the sense of family companies, trusts, uncles, aunts, etc.

- Contingent claims are entitled to vote at the Part X meeting. Claims which cannot be ascertained are not entitled to vote.

- Are there carried forward tax losses which you wish to preserve? If so, the type of administration should be carefully considered and appropriate tax advice sought.

- There may be other assets of the debtor which would not normally be available in a bankruptcy scenario which can be proffered to creditors. Alternatively funds may be available from third parties.

- Investigation into the debtor's past business affairs and also potential examination pursuant to Section 81 of the Bankruptcy Act can be avoided subject to the type of administration sought.

- A debtor can avoid the restrictions on carrying on business and incurring credit which would normally be applicable whilst an undischarged bankrupt.

- Various contingent liabilities may be crystallised in the sense that they are approved within the realms of the Part X. Of particular relevance for company directors for example are the provisions of Section 592 of the Corporations Law dealing with Insolvent Trading.
- In considering creditors claims and right to vote, a secured creditor, (that is, secured in the sense of holding security over the assets of the debtor), must quantify the value of their security and deduct same from the debt outstanding. The balance is the debt for the purpose of voting. If security is held by a debtor over third party assets irregardless of whether the claim against the debtor is pursuant to guarantees or not then the total amount of the debt outstanding by the third party can be voted and proved in a Part X administration.
- Consider whether related party creditors are prepared to waive their right to dividend under the Part X. This can provide a multiplier effect of benefit to other creditors and thus the attractiveness of the Part X, without increasing the burden on the debtor.