Session 3:

# Property Disputes, Insolvency Risk & Water Act Claims

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# Overview

Insolvency framework under the *Corporations Act 2001* (Cth)

Voluntary administration and liquidation

How can local government protect itself?

Ipso facto regime

# Current Economic Climate

## Probuild in administration as South African parent calls time

Michael Bleby and Nick Lenaghan

Updated Feb 23, 2022 – 6.24pm,
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Building contractor Probuild has become the largest casualty of Australia's increasingly pressured construction industry, after its South African parent appointed administrators after propping it up by 2 billion rand ($132.1 million) over the past four years.

## Winners emerge from building sector collapses

Michael Bleby *Senior reporter*

Apr 23, 2023 – 7.00pm

Expansion-hungry contractor Roberts Co is eyeing schools projects that belonged to failed Victorian commercial builder Lloyd Group to grow further in the southern state, showing that the construction crisis is creating opportunities for deep-pocketed companies to pick up work cheaply.

## Probuild collapse could be just the start in a 'broken' system

The collapse of builder Probuild shows how a broken system of contracting has built up in Australia, where too much risk is taken on for too little return.

Credit: Australian Financial Review
**Clippings taken from paid subscription*

<https://www.afr.com/property/commercial/probuild-in-administration-as-south-african-parent-wbho-pulls-the-plug-20220223-p59z0b>

<https://www.afr.com/property/commercial/winners-emerge-from-building-sector-collapses-20230420-p5d24e#:~:text=Lloyd%20Group%2C%20a%20Melbourne%2Dfounded,Porter%20Davis%20fell%20into%20liquidation>

<https://www.afr.com/chanticleer/probuild-collapse-could-be-just-the-start-in-a-broken-system-20220224-p59zh0>

# What is insolvency?

Insolvency occurs when a company or person cannot pay its debts when they fall due for payment


Common insolvency procedures available to companies under the *Corporations Act 2001* (Cth) include:

- Receivership
- Voluntary administration
- Liquidation
  - voluntary liquidation
  - compulsory liquidation
  - simplified liquidation
- Persons (including partnerships) can be made bankrupt

# Voluntary Administration and Liquidation

## Voluntary Administration

- Independent registered liquidator takes full control of the company.
- **Three ways an administrator can be appointed:**
  1. By board resolution;
  2. A liquidator or provisional liquidator of the company may appoint an administrator; or
  3. A secured creditor who has security entitlements may appoint an administrator if the security interest is over the property and enforceable.

## Liquidation

- The affairs of a company are being wound up and its business and assets are valued.
- A company may be voluntarily wound up or if the company is insolvent, by its creditors or by a Court Order.
  - *Voluntary liquidation* – occurs where the members of a company agree that the company be wound up.
  - *Compulsory liquidation* – where a court appoints a liquidator (usually because a company has not been able to pay its debt).
  - *Simplified liquidation* – a streamlined creditors' voluntary winding up for companies with liabilities under $1 million.

# How can local government protect itself?

**Local government can protect itself the following ways:**

- Performance security
  - Bank guarantees, insurance bonds, retention moneys
  - Parent company guarantee
- Payment for off site goods or materials
- Personal Property Securities Register (PPSR)
- Termination rights

# Security

Procurement contracts commonly require the contractor to provide a form of performance security.

**Common forms of security:**

- Commonly bank guarantee, insurance bonds or cash retention
- Parent company guarantees

**Tip**: Who is giving the guarantee and what is their credit rating?

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Procurement contracts commonly set the rules for having recourse or calling on security.

- Council may call on security if the contractor fails to fulfil its obligations under the contract

**Tip**: When can Council call on security? Is notice to the contractor required?

**Tip**: Is the security unconditional and on demand?

# Parent company guarantees

Construction contracts can include a requirement for the parent company of the contractor to guarantee the performance of the contractor if the contractor fails to perform.

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Allows council to pursue a claim against the parent company where the contractor company defaults.

# Payment for off site goods or materials

Contractors can request payment for goods and materials before delivery.

Risk is a contractor becomes insolvent before the goods and materials are delivered, Councils may have a weaker priority claim over the goods in an insolvency.

Councils can protect themselves in these circumstances by:

- Requiring security for the advanced payment;
- Transfer of title to the council upon payment; and
- Register the security interest on the *Personal Property Securities Act 2009* (Cth).

# Personal Property Security Register

Council may secure a “security interest” it has in “personal property”

Personal property includes things that are not attached to the land

- Does not apply to building works
- May include goods or materials not yet incorporated into building works

Councils should consider whether the need to register on the PPSR a security interest they have under the contract

This is an issue when a party tries to claim ownership of property, but another party has a superior claim under the Personal Property Securities Act legislation.

**TIPS**

- Register personal property on the PPSR
- Don’t be put off by the administrative burden

# Termination

Council may be entitled to terminate the contract if the contractor becomes insolvent

Termination allows Council to claim damages

Council can then engage a new contractor to complete the work/service/supply of goods and claim the extra costs as damages

If the Contractor is insolvent, recovering damages may be limited to the value of the performance security under the contract

- Insolvency risk is transferred to the bank / insurance company / parent company that is providing security

Rights to terminate for insolvency are now subject to the “ipso facto” regime under the Corporations Act that provides “safe harbour” for certain companies while they are insolvent

# Ipso facto regime

An ipso facto clause allows a party to the contract to terminate or modify the operation of the contract where the opposing company is undergoing a specified insolvency event.

The Corporations Act now includes a regime that imposes a temporary stay on parties who wish to suspend or terminate their contractual obligations on this basis.

**Exceptions:**

- *Corporations Regulations 2001* (Cth)
- *Ministerial Declaration Corporations Amendment (Stay on Enforcing Certain Rights) Declaration 2018* (Cth)

They include:

- A significant exception is a step-in right, meaning that the principal can take the works out of the contractor's hands upon the insolvency event and assign the works to another company.
- This effectively bypasses the ipso facto regime and helps councils in situations where their contractor is insolvent.

ipso facto

Adverb (ip-so-fak–toh)

# Key takeaways

Insolvency can be an unexpected and turbulent process

Steps can be taken to mitigate risks

TIPS

- ❑ Make sure you consider the following in any procurement contract:
  - o Is Council making payments to a Contractor before it receives the goods / services / works?
  - o If the Contractor goes insolvent will Council be out of pocket?
  - o Security in the form of a bank guarantee, insurance, cash retention, or parent company guarantee
  - o If you pay for goods or services in advance, ensure your interest is protected.
- ❑ Consider whether you need to register any interests and securities on the PPSR.
- ❑ Check to see if an exception to the ipso facto regime applies.