



To Take or Not to Take the Possible Preference? That is the Question!

We get asked to address this issue frequently.

For those with little exposure to the litigation process the answer in our view is always **“Take the payment and fight about is later”**.

A lot may happen that is not easy to predict. For starters the company may just survive, or for at least the 6 month time restraint. You never know, the Liquidator also just might miss the possible preference, not that it is likely.

Your client may have the requisite defences in any event or the Liquidator just may not be able to prove his case.

Even if the Liquidator’s case is strong, he may not have the funds to finance the action and the costs of a possible defeat, which makes a settlement for less than the full value of the preference likely.

When a Voluntary Administrator is appointed and creditors are asked to vote on a proposal for a Deed of Company Arrangement, they need to be aware of how their account has been conducted with the company and whether any payments within 6 months prior to the appointment could be subject to a preference action before they vote against any proposal and for liquidation.

The first thing a Liquidator has to prove is that the company was insolvent at the time or as a consequence of a possible preference. This is not always easy, even where all source documents are available as accounts for companies at the time of liquidation are rarely written up to date and the costs of reconstructing the records may prove prohibitive. It is often something that needs to be addressed after the action has been commenced.

The Liquidator also has to prove that if the company had been wound up at the time of making the subject payment that the recipient received more than all other creditors would have received had the company been wound up at that time. This is also no simple task if the books and records are in disarray.

In addition, the Liquidator then needs to be able to refute the creditors various defences being:

- The payments were received in good faith;
- There was no reason to suspect the company was insolvent;
- The running account argument (a la Compass Airlines); and
- The payments were not for valuable consideration.

When you look at the debt collection processes of businesses from the Liquidator’s perspective there is a tendency for the knowledge of the creditors at the time to be broadcast. This not only telegraphs the existence of the preference but makes it easier for the Liquidator to refute the defences normally available to the creditor.

Getting the money and not broadcasting the issue is a bit of a trade off. Some suggestions are:

- Jump on the slow payers early;
- Do as much of the collection process by phone where possible;
- Don’t accept round dollar figures. Make sure specific invoices are paid each time;
- Stop supply early until the account is brought into order; and
- Try to avoid loud stickers and stamps normally used as friendly reminders

As ever we welcome all your enquiries.



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