PAPER 1

RECEIVERS

Their Appointment, Their Duties
And Their Liabilities

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Qualification of a Receiver

The Companies Act, 1955 makes no reference to any special qualifications necessary for a person who is to act as receiver. Indeed, the only references are negative ones, referred to in Sections 342 and 343 which state that neither a body corporate nor an undischarged bankrupt may be appointed as a receiver.

From a practical angle a receiver must have sound financial and business experience and the ability to control a company until it is either rehabilitated or its assets realised to the best advantage. The work is both exacting and time consuming and any person approached to act should ensure that he can devote adequate time to the assignment.

APPOINTMENT OF RECEIVERS

There are a number of situations in which receivers may be appointed and the most common is pursuant to a power contained in a debenture.

Debentures usually contain a number of provisions enabling a receiver to be appointed, the most common of which is the power to appoint a receiver immediately after default is made in complying with a demand for the repayment of the advance.

The rights, powers and duties of a receiver are determined by two documents, firstly the debenture itself and secondly the instrument of appointment. The receiver must satisfy himself that both documents have been properly drawn, executed and are valid in all respects and must acquaint himself with the powers and duties contained therein.

If either the deed of appointment or the debenture is unsound, the receiver may be regarded as a trespasser and become personally liable on contracts undertaken in the name of the company or for assets converted into cash.
To avoid this possibility and for advice on other legal matters which will inevitably arise during the course of the receivership the receiver should instruct a capable solicitor to assist him. The solicitor should be a specialist in company and commercial law, preferably independant of the debenture holder and one who is prepared to make himself readily accessible.

**INDEMNITY**

A receiver is personally liable for all contracts into which he enters and for any losses sustained while carrying on the business.

He will of course have a right of indemnity out of the assets but if they are insufficient he could be faced with a personal loss.

Accordingly it is wise, in all cases, to obtain an indemnity from the debenture holder, particularly where the business is to be continued at the request of the debenture holder for whatever reason.

**NOTICE OF APPOINTMENT**

Section 109 (1) of the Companies Act, 1955 requires the person making the appointment to give notice of the appointment to the Registrar of Companies within seven days. While the responsibility for giving notice under Section 109 (1) is placed on the person making the appointment the receiver should satisfy himself that this provision of the Act has been complied with.

**Notice to the Company of the receiver's appointment and statement of affairs**

Upon his appointment the receiver must forthwith notify the company of his appointment (Section 348 (1) (a) ), by presenting formal notice to the head office of the company. Where the company has a number of branches, notice must be given to each branch. Contemporaneously, with the giving of the notice of appointment to the company's officers, their attention should be drawn to the provisions of Section 348 (1) (b) of the Act which requires the directors and secretary to furnish to the receiver within fourteen days or such longer period as the receiver shall allow, a statement in accordance with the provisions of Section 349 of the Act which in the prescribed form, is a statement concerning the affairs of the company. This statement must include full details of all the assets and liabilities of the company. The
preparation of such a statement is not easy as considerable detail is required in all sections and especially those relating to the liabilities. The possibility of a receiver's appointment coinciding with the end of a regular accounting period is remote, and thus the difficulties of the preparation of the statement are greatly increased. Nevertheless the information contained in the statement is vital for it includes details of the assets for which a receiver is required to account, and of the liabilities with which he must deal, including their relative priorities.

Difficulties may arise where the company does not employ its own full-time accounting staff and Section 349 (3) provides for a reasonable payment to be made of the cost of the preparation of the statement, which must be completed as soon as possible.

Section 348 (1) (c) requires the receiver within two months after the receipt of the statement of affairs to deliver a copy to the Registrar, together with any comments he sees fit to make thereon. Copies of the receiver's comments and of the statement of affairs must also be sent to the company, the trustees for the debenture holder, if any, and to all debenture holders.

Frequently assets are listed in the statement at book value which bear no relation to their realisable value. If so the receiver should comment drawing attention to the effect which any loss on realisation will have on the sum available, after payment of preferential creditors, to debenture holders, unsecured creditors and possible shareholders. If there is a genuine reason to believe that the company's position is not as favourable as shown in the statement of affairs, the receiver would be wise to comment accordingly.

In the initial stages of all receiverships there are certain matters which must be attended to without delay and there are often special problems on which the receiver's advice will be sought. It is important to prepare a programme covering matters requiring the receiver's attention to ensure nothing important is missed.

In most instances a receiver will elect to continue trading at least until he has established the company's financial position and has decided whether or not it is in the best interest of all creditors to attempt to trade the company out of its difficulties, or alternatively sell the business as a going concern. Under these circumstances he should at the earliest opportunity
speak to the staff and explain:-

1. That he has been appointed to protect the rights of the debenture holder.
2. That he is now responsible for the management and control of the company and has taken all the powers of management previously held by the directors.
3. That his appointment does not necessarily mean that the company will close down (providing this is the case).
4. That his appointment effectively freezes amounts owing to creditors and provides a breathing space in which to take stock of the position and decide on the company's future, and that this will take some time.
5. That they the staff will be advised of any decision affecting their future as soon as possible, and that in the meantime their help and assistance is essential to the company's future and the future of their employment.

This is a critical step. The staff will probably be upset by the turn of events, uncertain of their future and in a state of indecision.

The receiver must now accept full responsibility for the conduct of the company's affairs. He must take certain basic steps without delay. They are:-

1. Instruct all staff that the words 'in receivership' must be added after the company's name on all letters, invoices, statements and any other documents on which the company's name appears.
2. See that all existing bank accounts are closed and that new accounts are opened in the receiver's name.
3. Arrange for a complete physical stock take as at the date of his appointment.
4. Review all insurance policies to ensure that the assets and third party risks are adequately but not excessively covered.
5. Give formal notice to all creditors of his appointment advising that he will accept liability only for goods and services supplied against his written order.
6. Instruct the staff that goods must not be accepted or commitments undertaken except against his order. Very clear and firm instructions must be given to staff on this particular question. Any commitments which the staff enter into are made on behalf of the receiver and are commitments for which he may become personally liable.
7. Make adequate provision for safe custody of all assets.

8. Give notice to the staff that their contracts of employment are terminated and offer them re-employment on a weekly basis or longer period where necessary. This is perhaps the most difficult task immediately facing the receiver. Obviously, if he is going to carry on the business he will need a willing and loyal staff. He will immediately be involved in making a host of decisions in technical and commercial areas where he may have little or no experience and he will have to rely on the goodwill and advice of senior staff. It is an area requiring tact and understanding where maintenance of goodwill is essential.

9. Advise debtors who are also creditors that while they may be entitled to offset accounts relating to the period prior to receivership no such rights exists in respect of unsatisfied pre-receivership accounts against goods supplied to the receiver.

10. Set up an adequate system of control for the business and establish adequate security including control of keys, cash, stocks, etc.

11. Take possession of the common seal, minute book, certificate of title and other documents relating to the ownership of the company's assets.

12. Where the company is a licenced wholesaler or manufacturing retailer give notice of the appointment to the Comptroller of Customs.

13. Write to the company's customers advising that the company is going to continue to trade in receivership. Remember sales at an adequate profit margin will be of vital importance.

14. Where the company has plant, equipment or vehicles on lease and the receiver wishes to continue to use the items on lease, he should however, advise the lessors in writing that he will accept no other liability whatever under the lease. It is necessary to do so to avoid the risk of incurring cancellation charges which are written into most leases.

15. Advise the Directors that they remain responsible for holding meetings as required by the articles, registration of share transfers and filing of Annual returns.

This list is not exhaustive and each case must be carefully examined to see that nothing of importance is omitted. Once these basic steps have been taken the receiver should review without delay the company's financial position and consider its future. As all pre-receivership creditors accounts are deferred, normally a period of four to six weeks will elapse before the first payments are due to the receiver's creditors. This gives him an opportunity to collect some of the debts due to the company to meet current outgoings. He will have to decide whether or not receipts from cash sales, debtors, cont-
tract payments etc., will be sufficient to pay wages and other immediate out-
goings. Once the short term financial problems have been covered he should consider providing cash funds from sources such as a reduction in stocks and debtors, sales of surplus assets, etc. Of course any cash surplus will be reduced by the amount of any capital commitments such as hire purchase payments and reductions in mortgage principal.

A receiver must consider all existing contracts from a cash angle. He must establish whether or not cash receipts are likely to exceed the cost of completion. If not the receiver should not take up the contract and must ensure that no further costs are incurred.

If the receiver decides that the business cannot be continued indefinitely it may be desirable to carry on for a limited period to either:-

1. Negotiate a more favourable sale on the basis of a going concern.

2. To complete contracts in progress which will yield a cash surplus in excess of the cost of completion.

If however, the business can only be carried on at a loss then obviously the period on continuance must be very limited.

Obviously, making a decision on this point is relatively urgent and while the receiver is making up his mind he must carry on in a cautious manner. He must always bear in mind that the receiver's primary duty is to realise sufficient to satisfy the amount owing to the debenture holder and thereafter to terminate the receivership as quickly as possible. In carrying on the business a prudent receiver having regard to the interests of all creditors will exercise his powers wisely and not recklessly.

**COMPANY TRADING WHILE IN RECEIVERSHIP**

The position relating to the carrying on of a company's business by a receiver appointed out of Court is discussed in 'Palmer's Company Precedents' (16th Edition 1962) Part III page 404 where the following statement appears:-

Prima facie a receiver of the company's property is not entitled to carry on the business of the company but very commonly the debentures or trust deed empower him to carry it on.
Where the power is so conferred he may do whatever is reasonably necessary for carrying on the business, including the buying and selling of goods, the employment of labour and the incurring of debts and liabilities; and even though in the result loss is sustained, he will be entitled to indemnity, and the mortgages for whom he acts will be entitled to bring the expenses of receivership into account as against subsequent encumbrances and the company. (Bompas v. King (1996) 33 Ch.D279).

Usually the powers conferred on a receiver by a debenture include an authority to carry on the business of the company. Although the receiver is less likely to incur personal liabilities by closing the business down and selling the assets piecemeal the assets may not be realised to the best advantage. In recent times it has become more widely accepted that the appointment of a receiver need not necessarily mean the death knell of the company.

A survey of the company's trading position may indicate clearly that there are sound reasons for carrying on the business in the interest of all creditors, both secured and unsecured. However, before such a decision is acted upon, approval thereof should be obtained from, firstly, the debenture holder and secondly, the unsecured creditors who are the group most likely to benefit from a successful receivership.

Apart from a general consideration of trading conditions, the demand for the products, the company's ability to produce profitably at competitive prices, and the availability of raw materials and labour, particular attention should be directed to the current financial position. That is, whether or not receipts from cash sales, debtors, contract payments etc., will be sufficient to pay wages and other cash outgoings.

So far we have considered only the position where sufficient funds are available to the receiver from the company's own resources to meet normal outgoings. This will not always be the case, and it may be necessary, if the business is to continue, to raise a loan probably by way of bank overdraft to finance the company's trading. The consequences and responsibilities associated with the borrowing of funds are very complex. Before taking such a decision the receiver, must obtain an opinion from his legal advisers.

SALE OF REAL PROPERTY

Where it is proposed to realise the assets forming the security and such assets
include land or an interest in land, the debenture holder is required, pursuant to Section 92 of the Property Law Act, 1952, to give one month's notice to the owner of intention to sell. The land transfer office will not register the transfer unless satisfied that the required notice has been given.

THE RECEIVER IN RELATION TO THIRD PARTIES

1. **Directors**

   The receiver is responsible for the management and general control of the company's affairs from the date of his appointment, and is given all the powers of management previously held by the directors. There are, however, certain matters for which the directors are still responsible, which include the holding of meetings are required by the Articles, registration of share transfers and filing of annual returns.

2. **Execution Creditors**

   When a floating charge has crystallised into a fixed charge, a receiver, who has been appointed pursuant to powers contained in a debenture, is entitled to take possession of all the property comprised therein. Prior to crystallisation the mere existence of a floating charge does not prevent a judgment creditor from issuing execution against the property of the company subject to the charge. However, once a receiver has been appointed, a judgment creditor cannot prevail as against the receiver unless his execution has been completed at that date. In these circumstances the bailiff would be required to account to the receiver for the proceeds of the sale of any property seized prior to or after the date of the receivership unless settlement had been made with the judgment creditor prior to the date of the appointment.

3. **Landlord**

   Arrears of rent as such are not preferential claims; however when rent is in arrears the landlord may have the right to terminate the lease and the receiver may be compelled to pay the arrears to protect the lease.

   If a landlord obtains judgment for rent due and issues execution under this judgment, he is in the same position as any other execution creditor. Where, however, he proceeds under the Distress and Replevin Act, 1908, he has higher rights. For example, if he enters into possession under his distress before a receiver is appointed or the charge otherwise attaches, the distress takes priority as against the debenture holders, even though
it is not completed by sale.

4. **Hire Purchase Agreements**

The ownership under hire purchase agreements does not pass to the hirer until such time as the final instalment has been paid, and accordingly, unless the receiver pays the instalments as they fall due, the owner of the chattels held under hire purchase agreements can generally resume possession.

**CREDITORS**

1. **Preferential payments**

Section 101 of the Companies Act states, inter alia, that where a receiver has been appointed on behalf of the holders of any debentures of a company secured by a floating charge, and the company is at the time of such appointment not in the course of being wound up, the debts which in every winding up are, under provisions of Part IV of the Act relating to preferential payments, to be paid in priority to all other debts, shall be paid out of any assets coming into the hands of the receiver or other person taking possession of such assets, and such payments shall be made in priority to any claim for principal or interest in respect of the debentures.

This section refers to floating charge debentures. In the case of fixed charge debentures no such preferential rights apply.

The preferential payments are set out in Section 308 of the Act, and are the same both for receiverships and liquidations.

Preference is given to salaries, wages and holiday pay due to any servant or worker up to a maximum amount of $400 to any one claimant and for a period not exceeding four months prior to the appointment of a receiver. This provision does not extend to directors' fees which are not entitled to any preference.

2. **CLAIMS ON WHICH PREFERENCE IS CONFERRED BY OTHER ACTS**

(a) **Sales Tax**
Section 6 of the Sales Tax Amendment Act, 1933 requires a receiver of a licensed wholesaler or manufacturing retailer to send notice of his appointment to the Comptroller within fourteen days of his appointment. Under this section the receiver is required to set aside a sum sufficient to provide for sales tax payable or becoming payable and he become personally liable if he fails to do so.

(b) P.A.Y.E.

Section 31 (1) of the Income Tax Assessment Act 1957 provides that P.A.Y.E. deductions shall be held in trust for the Crown and shall form no part of the estate in liquidation. Section 31 (2) provides that the amount of tax deduction for the time being unpaid to the commissioner shall upon liquidation or upon the appointment of a receiver rank immediately after the debts referred to in Sub-section (1) of Section 308 of the Companies Act, 1955.

(c) Motor Vehicle Dealers Act 1975

Where a payment is made out of the Motor Vehicle Dealers Fidelity Guarantee Fund in settlement of a claim against a Motor Vehicle dealer the Motor Vehicle Dealer Institute Inc. shall be subrogated to the extent of the payment to all the rights and remedies of the claimant against the dealer. The amount that the Institute is entitled to recover from the defaulting licensee company shall be paid in priority to all other debts in accordance with para (d) of subsection (1) of Section 308.

(d) Land Tax

Section 220 of the Land and Income Tax Act, 1954 provides that land tax which has been assessed and has become due and payable shall be a charge on the land in respect of which it is payable. In a statement of affairs unpaid land tax should be shown as secured against the land in respect of which it is payable.

(e) Rates

Rates when struck constitute a charge upon the land. Unpaid rates should be treated in the same manner as land tax.

ORDER OF PREFERENTIAL PAYMENTS

The order in which preferential payments rank is:
1. The costs of realisation
2. Sales tax. Section 27 of the Sales Tax Act gives sales tax priority to the costs of the receiver.
3. The costs, including remuneration, of the receiver.
4. Salaries, wages, and holiday pay due to employees up to $400 to any one person and covering a period not exceeding four months together with all other sums required by any other Act to be included among debts which are to be paid in priority to all other debts in a winding up.
6. Amounts secured by debenture including, where debenture so provides, costs, charges and expenses of the debenture and, if applicable, a debenture trust deed together with trustees remuneration.

Section 11 of the Layby Sales Act and Section 31 (2) of the Income Tax Assessment Act, 1957 appear to be in conflict in that both provide for a preference second to the debts having priority under Section 308 (1). It has yet to be authoritatively determined which section has priority over the other.

When the company is also in liquidation, it is advisable for the receiver to obtain the liquidator's approval for any payments which he intends to treat as preferential.

UNSECURED CREDITORS

Although the receiver is not legally required to concern himself with unsecured creditors, they are the group of people, who in most cases, stand to gain or lose the most by carrying on the business. If it is intended that the business should be continued for the benefit of all parties, the receiver should call a meeting of all unsecured creditors to acquaint them with the situation and to obtain their approval to the course which he intends to follow.

Unsecured creditors may exhibit resentment when their accounts are deferred, particularly if there is a strong possibility that all or a major part of the amounts outstanding appear to be irrecoverable. Some may go to considerable lengths to persuade the receiver that, for various reasons their accounts should be given preferential treatment. All such claims must be carefully scrutinised and only those with a legal priority should be given preference. It is important to remember when considering creditor's accounts that time is on the side of the
receiver and hasty decisions should not be given. When it doubt seek a legal opinion. Even where creditors resort to legal action the matter is usually protracted giving the receiver and his legal adviser ample time for a full consideration of the claim.

**UNCALLED CAPITAL**

The power of a receiver to get in uncalled capital will depend whether or not the company is in liquidation.

If the uncalled capital is part of the security for the debenture the directors may be instructed by the Court to make a call and pay the proceeds to the receiver, or the Court may authorise the receiver to make the call.

However, when the company is also in liquidation the directors' powers to make calls are terminated and the liquidator is the only person empowered to act. The Court may either instruct the liquidator to make the call or authorise the receiver, on giving suitable indemnity to the liquidator, to make the call in the name of the Liquidator.

**LIABILITIES OF THE RECEIVER**

Section 345 (2) of the Companies Act, 1955 states that a receiver, appointed under powers contained in an instrument, shall be personally liable, to the same extent as if he had been appointed by order of a Court, for any contracts entered into by him in the performance of his duties except in so far as the contract provides otherwise and he is entitled in respect of that liability to an indemnity out of the assets. However, nothing in this sub-section limits either the right of indemnity which he had apart from the provisions of the sub-section, or his personal liability on contracts entered into without authority.

If a receiver appointed under a floating charge debenture, neglects to discharge the preferential creditors, he becomes liable. Likewise if appointed by the Court, he becomes personally liable if he does not carry our precisely the terms of Court Order.

The Receiver who is agent of a company may also render himself personally liable under the general law of agency. Firstly where he signs a contract,
as for example, a bill of exchange other than in his representative capacity and secondly for liability in tort.

THE LIQUIDATOR AND THE RECEIVER

It is not uncommon for a liquidator to be appointed while the receiver is still in office. In these circumstances the receiver must immediately cease trading as the liquidation automatically cancels his right of agency and he becomes personally liable as from that date in respect of any contract into which he enters.

On occasions where a company is in receivership and is going into liquidation it is suggested that the receiver should also act as the liquidator. Such a suggestion requires careful consideration, as there may be occasions where a conflict of interest will arise and a receiver should clearly resort to his solicitor for advice.

For example, where the debenture appointing the receiver was issued within twelve months of the date of winding up and was given for the purpose of securing a past debt, Section 311 of the Companies Act states clearly that except in so far as the debenture secures the value of the goods or advances made after the date of issue, the debenture, unless it is possible to show that the company was solvent at the date of the taking of the debenture, shall be inlaid as against the liquidator. Clearly in such circumstances there could be a conflict of interests.

The appointment of a liquidator does not displace the receiver and while he can no longer carry on the business his powers to realise the assets continue, subject of course to the debenture being enforceable against the liquidator.

RECEIVER'S ABSTRACT OF RECEIPTS AND PAYMENTS

The requirements of the Companies Act, relating to the filing of receiver's abstract of receipts and payments with the Registrar of Companies are.

1. Appointments under floating charge debentures. Section 348 (2) provides that the first statement must cover the period of the first twelve months from the date of appointment, and subsequent statements each succeeding
period of twelve months or to the date of termination. The statement must be filed within **two months** from the end of the relevant period or such longer period as the Registrar shall allow.

2. Appointments in all other cases. Section 350 provides that the first statement must cover the period of six months from the date of the appointment and each subsequent period of six months or to the date of termination. The statement must be filed within thirty days of the end of each period or such longer period as the Registrar shall allow.

**TERMINATION OF RECEIVERSHIP**

As soon as the receiver is in a position to pay off the debenture holder he should do so and terminate his appointment as soon as possible. He must satisfy himself that all claims and liabilities outstanding against him have been satisfied and if he has been trading he should advise all parties with whom he has had transactions that he is terminating the receivership and ask for a final statement of account. As a precaution he should obtain, if he has not already done so, a suitable indemnity from the debenture holder against outstanding liabilities.

If the company is also in liquidation the receiver must transfer and surplus assets he holds to the liquidator. He should arrange for the liquidator to accept any claims which may arise relating to the receivership, for say, a period of twelve months or, alternatively with the consent the liquidator hold a sum of money for a reasonable period to meet any claims arising within that period.

As soon as the amount owing under the debenture has been satisfied and any outstanding claims provided for or alternatively, all the assets have been realised and the proceeds paid to the debenture holder, the receiver must obtain a discharge from the debenture holder. He must file with the Registrar of Companies a notice of his ceasing to act within seven days and a final abstract of receipts and payments within two months.

A receiver of a company carrying on the business of a licensed wholesaler or manufacturing retailer, and licensed under the Sales Tax Act, must notify the Comptroller of Customs that he has ceased to act and pay any outstanding sales tax.
The foregoing is an introduction to some of the practical aspects which arise in most receiverships.

A receiver holds a position of trust and must have a basic understanding of the law which will enable him to recognise legal problems as they arise. It is of even greater importance to have the assistance and guidance of a solicitor well versed in the statutes and caselaw governing companies.

A receiver's work is exacting and demanding, it requires common sense and tact. But is interesting and rewarding.