

News with Clout

Providing Corporate & Personal Solvency Solutions

FORMAL PERSONAL INSOLVENCY SERIES - INSTALMENT 2 PART X PERSONAL INSOLVENCY AGREEMENTS

In this month's newsletter we consider the benefits of Part X - Personal Insolvency Agreements (PIAs) from the Debtors perspective.

PIAs provide some comfort for Debtors that they have not gone bankrupt despite being insolvent. Some people, generally of the older generations regard bankruptcy as having a stigma attached to it. Avoiding bankruptcy is really a cold comfort, as under all three formal personal insolvency administrations, the Debtors credit rating is tainted for 7 years and there is a permanent listing on the National Personal Insolvency Index (NPII) maintained by ITSA.

Part IX - Debt Agreements and PIAs have the same benefits in many areas. There is just the question of dollar figure thresholds that separate the two types of administrations. Under the thresholds, the Debtors affairs can be handled under Part IX, over the threshold and Part X will apply. The thresholds for assets and creditors is currently \$88,379.20 and for income \$66,284.40.

To recap the advantages of PIAs and Debt Agreements are that they provide the possibility of retaining assets where there is no equity that may be available for the benefit of creditors, particularly real estate. Under bankruptcy any potential equity (meaning equity that accumulates over time) is exposed for up to 9 years. In addition under bankruptcy the concept of after acquired property means any windfall that is possible in the three years from bankruptcy is caught by it and must be made available for the benefit of creditors.

Inheritance is a classic example. Under bankruptcy there is also an obligation, if a debtor's income surpasses certain thresholds, for contributions to have to be made to their bankrupt estate out of income. This applies over three years. Under the two other formal administrations if there is an improvement in earning capacity the Debtor usually keeps it.

Whilst the processes required to implement a PIA

are more involved than that of Debt Agreements, it is generally a very flexible concept in the commercial sense. The rule of thumb is that for creditor's approval to be obtained for a PIA they need to be looking at receiving a higher proportion of their debt than would be available under a bankruptcy.

Under Part X a proposed PIA, if it receives approval at the creditors meeting by a majority in number representing 75% in value present and voting at the meeting, all creditors are bound including the dissenting voters.

One example where PIAs have been successful in the past, for us, is where a development application for a rural residential subdivision had received council approval. The owner was insolvent as a result of a failed business. To have gone bankrupt would have meant the Trustee or the secured creditor would have had little choice but to auction the property with the approval intact. Comparative valuations and budget to finalise the development showed the likely net outcome for creditors was markedly better if they allowed the Debtor to complete the subdivision. With the support of the secured creditor it resulted in unsecured creditors receiving 95 cents in the dollar as opposed to about 30 cents. The debtor ended up with a surplus as well at the conclusion with which to start again.

Another example was where there was a sole trader whose business had no value and there was no equity in the assets. It had been sold to a related party and had a possible exposure under Section 120 of the Bankruptcy Act for a transfer for less than fair value if bankruptcy eventuated. What was offered under Part X was income and a share of profits which was shown to be achievable over a two year period and better than and less risk than bankruptcy and was accepted by creditors.

As ever we welcome all your insolvency enquiries.