

BUILDER INSOLVENCY AND FINANCIAL DIFFICULTY CREDITOR AND SUBCONTRACTOR SUPPORT

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Australia's building industry is facing exceptional challenges, and insolvencies are on the rise. When builders become insolvent, subcontractors and suppliers are often left out of pocket.

If you are providing subcontracting work and the builder you are completing work for becomes insolvent, it is essential you know what to do. This guide is designed to assist subcontractors if their builder becomes bankrupt or goes into voluntary administration or liquidation.

What is insolvency?

Insolvency is when a company or person is unable to pay debts when they are due.

Irrespective of whether the builder is a sole trader, a partnership, or a building company, they are unable to operate when insolvent.

Company Insolvency

If the building company is, or is likely to become, insolvent, then the building company may become subject to external administration.

When a construction **company** is unable to pay its debts, it often enters voluntary administration or the business is wound up through a liquidation process.

In some situations insolvency solutions are sought through a restructuring plan, the goal of which is to reach an arrangement with creditors for the continuation of the business.

The type of external administration depends on whether the building company is able to reach an agreement with the company's creditors to become solvent.

Individual Insolvency

If the individual builder is, or is likely to become, insolvent, the builder may apply for bankruptcy on the builder's own accord or be forced into bankruptcy by way of a petition commenced by one or more creditors'.

If the builder is a **sole trader or partnership** they may enter bankruptcy or enter into a Part IX (9) (also known as a Debt Agreement) or X (10) agreement (also known as a Personal Insolvency Agreement).

Bankruptcy is a legal process where an individual declares they are unable to pay their debts. It releases the individual from most debts, and a bankruptcy period normally lasts for at least three years.

A Part IX agreement is where an individual negotiates to pay a percentage of the combined debt over a period of time. The repayments are made to a debt agreement administrator, rather than individual payments to creditors. After the payments are completed and the agreement ends, the creditors can't recover the rest of the money owed.

A Part X agreement is a legally binding agreement between an individual and their creditors, and can be a flexible way to come to an arrangement to settle debts without becoming bankrupt. A trustee is appointed to take control of the affairs and to make an offer to the creditors. The offer may be to pay part or all of the debts by instalments or a lump sum

What action does QBCC take when a builder is, or is likely to become, insolvent?

To ensure public confidence in QBCC's licensing system and to promote security of payment, the QBCC's legislation contains provisions which prevent those responsible for poor financial management from running a business.

Practically speaking, this means that when a construction company has a liquidator, administrator or controller appointed; or is wound up, or is ordered to be wound up; QBCC will exclude the individual directors, secretary or influential persons from holding a licence.

Similarly when an individual who is acting as a sole trader or in partnership becomes bankrupt or enter into a Part IX or X agreement, the QBCC will exclude the individual from holding a licence.

QBCC confirms insolvencies with the Australian Securities & Investments Commission (companies) and Australian Financial Security Authority (individuals). Upon confirmation, QBCC follows a process that can result in suspending or cancelling the builder's licence, depending on the circumstances.

The process can include:

- Sending a formal written notice to any directors who hold a licence issued by QBCC, advising of potential suspension or cancellation of their individual licence;
- Assessing any submissions made by the licensee in response;
- In the event that no response is received, proceeding to give the licensee written notice of the decision to suspend or cancel the licence.

Red Flags and Warning Signs for Insolvency

If you suspect that the builder is insolvent, watch out for these signs:

- **Financial strain** – late payment, non-payment;
- **Communication breakdown** – lack of communication or transparency;
- **Delays** – frequent project delays or missed milestones.

What should I do if I suspect my builder is insolvent?

If you think that the builder may be insolvent, you should check their current status and obtain details of the insolvency practitioner:

- If the builder is a sole trader or partnership, conduct a Bankruptcy Register search with [AFSA Bankruptcy Register Search](#).
- If the builder is a company, search ASIC's register of companies at: [Search Company and Other Registers \(asic.gov.au\)](#)
- If you are not sure whether your builder is a company, sole trader or partnership, search both.

If the builder is insolvent, you may receive a letter from the insolvency practitioner appointed to administer the affairs of the builder notifying you of what has happened, providing you with information about what to do next, and inviting you to lodge a proof of debt if you are a creditor of the builder. Sometimes, you may not be contacted.

What do I do if I suspect my builder has entered a form of insolvency, but it is not reflected in the registers?

If you suspect the builder is insolvent, and you have a significant trading relationship, consider having a chat with a financial advisor or seeking legal advice. If you are owed money, lodge a monies owed complaint with the QBCC.

Ensure that you retain copies of all contracts, communications and relevant documentation with the builder to defend any claims down the track.

What should you do if your builder is recorded as insolvent in the register?

You should follow these steps:

(a) Make contact

If the builder is a company, make contact immediately with the insolvency practitioner that has been appointed to the builder. The insolvency practitioner may not be aware that you have engagement with the builder, or that you are owed money.

(b) Make a claim

If you are owed money by the builder you should consider lodging a claim (also called a 'proof of debt') using the relevant form obtained from the insolvency practitioner.

You can lodge a claim for debts, as well as contingent amounts owing, that have not yet been quantified. The builder may not ultimately have any money to pay a dividend to creditors. However, creditors who lodge a claim:

- receive reports about the affairs of the builder under external administration.

- participate in meetings to decide whether to change the insolvency practitioner with carriage of the external administration; and
- participate in meetings to decide whether to accept any compromise with creditors that may be proposed, or whether the builder should instead be made bankrupt or placed into liquidation.

Your claim may be rejected if there is insufficient evidence to support it. You should attach to the 'proof of debt' form copies of any relevant agreements, invoices, reports, photos or other supporting documents.

Where a building defect has been identified but not yet been remedied, or the builder's responsibility for the defect is disputed, you will need to supply the external administrator with sufficient information to enable a 'just estimate' of the builder's liability to be determined, in order to have your claim accepted.

You should consider obtaining legal advice as to how you might justify your claim. You may consider whether other creditors with similar claims (for example, other subcontractors) are willing to share the cost of preparing an expert's report that can be provided in support of each claim.

Appeal from rejection of proof of debt

The insolvency practitioner appointed to the builder may accept or reject, in whole or in part, your claim. There is a statutory mechanism to appeal the decision to a court. If you wish to dispute the decision, you should promptly seek legal advice.

Review of any proposed compromise with creditors

Both voluntary administrations and bankruptcies are sometimes resolved through a compromise with all or a subset of creditors. If the builder becomes bankrupt, the proposed compromise will be called a 'personal insolvency agreement'. If a building company goes into voluntary administration, the proposed compromise will be called a 'deed of company arrangement'.

If you have lodged a claim or 'proof of debt' in the external administration, you may be able to vote on whether to approve the compromise. You should carefully review the information provided by the external administrator in deciding whether the outcome under the proposed compromise provides you with a better outcome than the alternative (generally, bankruptcy or liquidation).

This is likely to be a function of the proposed compromise and the value of the assets otherwise available, if the compromise is not accepted.

If you think there are gaps in the information provided by the insolvency practitioner, or further inquiries should be made before creditors have to vote on the proposal, you should contact the insolvency practitioner's office and consider obtaining legal advice.

Disclaimer

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