

Inspector-General Practice Direction 10

IGPD 10 - Treatment of secured creditors in a Part IX debt agreement

1. Introduction

~~1.1 The Bankruptcy Legislation Amendment (Debt Agreements) Act 2007 altered the manner in which secured creditors are treated under a Part IX debt agreement.~~

1.21 The parties to a debt agreement must be aware ~~that these changes are~~ that the manner in which secured creditors are treated under a Part IX debt agreement is relevant to the formulation of proposals, the completion of debt agreement forms, the processing of debt agreement proposals and the assessment of voting upon proposals. Secured creditors ~~They~~ must be taken into account by administrators when working with debtors to prepare proposals.

~~Creditors should take these changes into account when considering whether or not to vote on a debt agreement proposal.~~

1.23 Debt agreement administrators are encouraged to enter into discussions with secured creditors when formulating proposals in order to address some of the issues raised below.

1.34 Creditors and debtors need to consider if there is a possibility that during the debt agreement a secured creditor may repossess their security and if there is likely to be a shortfall on the asset.

1.45 Information such as the payment history of the debtor in respect of their secured creditors can provide an indication as to the likelihood that the debtor will fail to continue to make direct payments to secured creditors, that the secured creditor will repossess their security and the likelihood of a shortfall.

1.56 Administrators ~~need to be alert~~ when assisting debtors to prepare a debt agreement proposal, should ensure disclosure of ~~to disclose~~ the up to date position with regard to secured creditors so that the body of creditors can make an informed decision. The possible impact of the issues raised below reinforces the importance of full disclosure when completing debt agreement documentation, in particular providing, when necessary, additional explanations of matters relating to secured creditors in the debtor's explanatory statement.

1.67 Administrators will need to have regard to continuing payments to secured creditors when complying with their obligation pursuant to section 185C to certify that they have reasonable grounds to believe that the debtor is likely to be able to discharge the obligations created by the agreement as and when they fall due. In cases where the debt agreement's 'proposal's percentage'¹ exceeds the 'prescribed percentage' under the Bankruptcy Act 1966 (the Act), an administrator will need to certify that they are **satisfied** that the debtor is likely to be able to discharge the obligations created by the agreement. Note that ~~the threshold~~

¹ A 'proposal percentage' is the total payments under the agreement plus a low income debtor amount as a percentage of a debtor's after-tax income. The 'prescribed percentage' is determined by the Minister by legislative instrument. Further explanation can be found in IGPD13 Debt agreement administrators' guidelines to certification requirements.

to prove of 'satisfied' is a higher than the threshold than that of 'reasonable grounds to believe'.²

2. Who is a secured creditor?

2.1 For a debt agreement entered into before 30 January 2012, a secured creditor means a person holding a mortgage, charge or lien on property of the debtor as a security for a debt due to them from the debtor.

2.2 For a debt agreement entered into on or after 30 January 2012, a secured creditor means:

- a. in the case of a debt secured by a Personal Property Securities Act (PPSA) security interest—the PPSA secured party in relation to the interest, if the interest:
 - i. arose as security for the debt
 - ii. is perfected (within the meaning of the PPSA) or
- b. in the case of any other debt—a person holding a mortgage, charge or lien on property of the debtor as a security for a debt due to him or her from the debtor.

2.3 Secured creditors, unlike unsecured creditors, possess rights against specific assets to ensure payment of their debt. Normally these rights ~~only arise~~ are only exercised if the debtor is in default in making payments to the secured creditor. Whether a creditor is secured will depend upon whether they legally have rights to enforce their debts against specific assets, not whether in practice they can or will enforce those rights. In relation to a debt secured by personal property (within the meaning of the PPSA, e.g. cars, boats, crops, inventory, intellectual property) the security interest must be perfected in accordance with the PPSA and arise as a security for a debt.

2.4 A secured creditor may be fully or partially secured.

3. How much a secured creditor can vote for

3.1 Sections 185EC, 185MC and 185PC provide that a secured creditor may vote for the unsecured portion of their claim. A secured creditor is taken to be a creditor for voting purposes only to the extent by which the amount of the debt owing to the creditor exceeds the value of the creditors' security.

Example 2

Mr White has a \$10,000 debt to ABC Finance. The debt is secured over Mr White's motor vehicle, which has a market value of \$9,000. Mr White submits a Part IX debt agreement proposal. ABC Finance is able to vote on the proposal in the amount of \$1,000.

3.2 Any decision by AFSA's Debt Agreement team (DAT) on the amount for which it allows a secured creditor to vote is not binding on a debt agreement administrator when the administrator assesses the extent to which a secured creditor is entitled to dividends under the debt agreements.

² ~~From 27 June 2019 for proposals lodged on or after that date~~ [For debt agreement proposals lodged with the Official Receiver on or after 27 June 2019 check]

4. The ~~extent~~ amount a secured creditor can vote for

4.1 Subsection 185C(2) has the effect that if a secured creditor does not realise their security while the agreement is in force, the creditor is taken to be a creditor to the extent by which the amount of the creditor's debt exceeds the value of the creditor's security at the time when the acceptance of the proposal for processing is recorded on the National Personal Insolvency Index.

Example 3A

At the time that she enters into a debt agreement, Ms Green owes \$20,000 to a finance company, XYZ Finance. XYZ has a bill of sale over Mrs Green's \$5,000 motor vehicle. Ms Green's debt agreement administrator determines that the size of XYZ's claim in the debt agreement (for the purpose of XYZ sharing in any dividends) is \$15,000 (i.e. \$20,000 - \$5,000).

4.2 Subsection 185C(2) also has the effect that if a secured creditor realises their security while the agreement is in force, the (formerly secured) creditor is taken to be a creditor only to the extent of any outstanding provable debt ~~remaining outstanding~~. Any interest accrued on the debt after ~~the~~ acceptance of the proposal for processing is recorded on the National Personal Insolvency Index, is not provable.

Example 3B

As above, except that XYZ takes possession of and sells the motor vehicle after 2 years, but before the debt agreement is completed. After the realisation of the motor vehicle and the application by XYZ of the sales proceeds to the debt owed, Ms Green still owes XYZ the sum of \$8,000. Ms Green's debt agreement administrator amends the amount of the unsecured debt of XYZ in the debt agreement ~~of XYZ~~ from the original amount of \$10,000 to the new amount of \$8,000.

Dividends to all creditors are adjusted to ensure that all creditors are paid the same dividend rate.

4.3 If the asset is repossessed at some time during the debt agreement, all parties need to appreciate that the debtor's expenses may then become less than those disclosed at the time that the proposal was made. The debtor may have more income available to pay towards the debt agreement—allowing the debt agreement to be paid out by the debtor in advance of the original schedule for payment or enabling a variation of the agreement to increase the amount offered by the debtor as ~~(so long as the variation proposal percentage does not exceed the prescribed percentage under the Act)~~.³

4.4 A debt agreement administrator must make their own assessment of the amount in respect of which a secured creditor is entitled to participate in a debt agreement. The administrator should not merely accept ~~either~~ the debtor's figures, the amounts disclosed on a secured creditor's claim and vote form (CAV) statement of claim and voting (SOCAV) or the DA team determination in respect of a (CAV) SOCAV. However, an administrator should

³ [From commencement of amendments on 27 June 2019 or debt agreement proposals and subsequent variation proposals lodged with the Official Receiver on or after 27 June 2019](#)

have due regard to this information, together with any additional information obtained by the administrator.

Example 4

Mr Red claims to be a secured creditor of Ms White. In her statement of affairs, Ms White discloses a debt of \$15,000 to Mr Red, secured on a \$10,000 boat. In his SOCAV, Mr Red claims a debt of \$16,000 from Ms White and claims that the boat is worth only \$8,000. ~~DAI team~~ assesses Mr Red's claim as a debt of \$16,000 secured on a \$9,000 boat (relying on the Red Book value) and allows him to vote in the amount of \$7,000. Subsequently, once the agreement is established, the administrator assesses the above information, together with further documents provided by the debtor and determines that Mr Red can participate in the debt agreement in the amount of \$7,000. This assessment is based on an assessed debt of \$15,000 secured on an \$8,000 boat.

4.5 A secured creditor can choose not to accept payments under a debt agreement and instead rely on direct payments made by the debtor. A secured creditor is in a different position to unsecured creditors in that they retain their rights of direct enforcement in respect of their security. Retention by the debtor of the property subject to security may necessarily involve [the continuation of](#) direct payments to the secured creditor ~~being continued~~.

4.6 For example a secured creditor could choose not to accept any dividends under a debt agreement. The secured creditor could choose to only assert its right to participate in dividends under the debt agreement if the debtor defaults and the secured creditor subsequently repossesses its security and suffers a shortfall.

4.7 It should be recognised that a situation such as that referred to in the above example may add additional complexity to the administration of a debt agreement. A secured creditor may choose to decline to accept any dividend payments under a debt agreement, whether or not a debtor continues making direct payments to the secured creditor.

4.8 Irrespective of whether a secured creditor accepts dividends under a debt agreement, a secured creditor will still be a party to the debt agreement. Whether or not a secured creditor takes action to realise their security, the secured creditor is entitled to receive dividends if they so choose (and may do so without the need for any variation of the debt agreement). The debtor will still be required to disclose details of the secured creditor in their debt agreement documentation. The secured creditor will still be bound by the agreement and the secured creditor's debt will be released upon completion of the agreement (except in respect of their rights to deal with their security). A secured creditor can realise its security after the completion of a debt agreement but cannot pursue the debtor for any shortfall. This is the case whether or not the secured creditor has received any dividends pursuant to the debt agreement.

4.9 If it is anticipated that a secured creditor will not be accepting dividend payments, this should be disclosed by the debtor in their debt agreement proposal ~~or~~ and explanatory statement.

5. No entitlement to more than 100 cents in the dollar

5.1 Subsection 185C(2) also provides that creditors are not entitled to receive more than the amount of their provable debt.

5.2 Secured creditors generally receive payments other than pursuant to the debt agreement (such as by direct payments by the debtor or from the proceeds of repossessing secured assets). Administrators should ensure that payments are not made to secured creditors with respect to the unsecured portion of their claims, if the claims of the secured creditor have been satisfied in full.

Example 5A:

Mr Yellow owed a debt to XYZ Finance, secured ~~upon by~~ a motor vehicle. XYZ has been assessed as being entitled to receive dividends under Mr Yellow's debt agreement.

XYZ Finance seizes and sells the motor vehicle, leaving a \$2,000 shortfall.

Mr Yellow's debt agreement administrator proceeds to pay a dividend. The amount of the dividend to XYZ would normally have been \$3,000, however as there is only a \$2,000 debt remaining, XYZ is paid \$2,000 and the balance is distributed amongst the other creditors. XYZ receives no further dividends.

Example 5B:

Ms Grey owes \$5,000 to ZZZ Loans Ltd, secured ~~by~~ a vehicle valued at \$1,000. There are 50 weekly payments of \$100 remaining to be paid under the contract. Ms Grey maintains these payments during the term of the debt agreement.

Additionally a monthly dividend of \$100 is paid to the secured creditor pursuant to the debt agreement. The debt is paid in full after 40 weeks.

The DAA monitors the payments made and ceases dividends to ZZZ Loans Ltd after 40 weeks, in order to ensure that they are not paid more than 100c in the dollar.

~~6. Release of debt owed to a secured creditor~~

~~6.1 Generally, upon completion of a debt agreement, a debtor is released from any debts that would be released by bankruptcy. However, this release is subject to section 185XA which provides that nothing in the debt agreement regime affects the rights of a secured creditor to realise or otherwise deal with their security.~~

~~6.2 A secured creditor can realise its security after the completion of a debt agreement but cannot pursue the debtor for any shortfall. This is the case whether or not the secured creditor has received any dividends pursuant to the debt agreement.~~

76. Completion of the explanatory statement and statement of affairs

~~67.1~~ Section 185C imposes an obligation upon debt agreement administrators to certify that they had reasonable grounds to believe that all the information required to be set out in a debtor's statement of affairs and explanatory statement has been set out in those documents.

~~67.2~~ This obligation does not merely extend to ensuring that secured creditors are disclosed but also to ensuring that asset and debt values in respect of such creditors are accurately recorded.

~~67.3~~ The certification obligation in section 185C requires that a debt agreement administrator should not merely rely on the debtor's opinion as to the market value of assets upon which debts are secured, but should also ensure that there has been some kind of corroboration of the debtor's opinion. An appropriate level of corroboration will depend upon the nature of the asset and the circumstances of the case. A formal valuation is not necessarily required.

~~67.4~~ Examples of corroboration ~~might may~~ include but are not limited to: a review of the prices of similar properties listed for sale, the red book value of a vehicle, the administrators own personal knowledge. ~~Depending on the circumstances of the case, some of these examples might not be appropriate in a specific case.~~

~~67.5~~ ~~An~~ For an example of how the explanatory statement should be completed, see follows ~~in~~ figures 1 and 2.

~~8. The explanatory statement~~

Figure 1: Section C of the explanatory statement

C. Assets and Secured Creditors

Unsecured Assets – Description (eg. shares, real estate address details, vehicle details)		Estimated Total Value	Percentage Owned		
		\$	%		
		\$	%		
		\$	%		
		\$	%		
Secured Assets – Description (eg. shares, real estate address details, vehicle details)		Estimated Total Value	Percentage Owned		
1	2010 Nissan (Secured against #2)	\$ 10000.00	100.0 %		
2	123 Fred Street, SYDNEY NSW 2000 (Secured against #1)	\$ 150000.00	100.0 %		
3		\$	%		
4		\$	%		
Secured Creditor Name	Secured Creditor Postal Address / Email Address	Reference/ Account Number	Joint Debt?	Amount Owed	Surplus/ Shortfall
1	COMMONWEALTH BANK 21 Walsh Close, ILLAWONG NSW 2234 Creditor Type Bank Nature of debt House Mortgage	12345678 Up to date	<input checked="" type="checkbox"/>	\$ 100000.00	\$ 50000.00
Participating in dividends on estimated shortfall? <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No					
2	ALLIANZ AUSTRALIA PO BOX Q1015, PACIFIC FAIR QLD 4218 Creditor Type Other Nature of debt Not Applicable	987654321 Up to date	<input checked="" type="checkbox"/>	\$ 12000.00	\$ -2000.00
Participating in dividends on estimated shortfall? <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No					
3			<input type="checkbox"/>	\$	\$
Participating in dividends on estimated shortfall? <input type="checkbox"/> Yes <input type="checkbox"/> No					
4			<input type="checkbox"/>	\$	\$
Participating in dividends on estimated shortfall? <input type="checkbox"/> Yes <input type="checkbox"/> No					
Item C - Total amount of unsecured shortfall				\$	2000.00

C. Assets, including shares, the debtor is keeping

Description	Value \$	Jointly Owned
Unit at 123 Fred Street, Sydney	190,000.00	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
2006 Proton Savvy	11,400.00	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Television	500.00	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No

Figure 2: Sections D and E of the explanatory statement.

D. Secured creditors including lease/hire purchase where debtor intends to maintain payments

Name	Phone No.	Account No.	Status <small>e.g. up to date, arrears, collector, leased vehicle, sublease</small>	Amount owed \$
1. ABC Bank	07 34534534	1111111	Arrears	164,000.00
2. D&E Savings & Loans	03 23423423	2222222	Up to date	14,990.00
3. Mr. Red's Rentals	02 12312312	3333333	Up to date	661.63
4.				
Assets held as security - description			Estimated value \$	Surplus/shortfall \$
1. Unit at 123 Fred Street, Sydney			190,000.00	26,000.00
2. 2006 Proton Savvy			11,400.00	(3590.00)
3. Electrical equipment			500.00	(161.63)
4.				

E. Unsecured debts List all creditors

Include unsecured portions of secured creditor debts after value or sale of security

Name of creditor	Phone No.	Account No.	Status <small>e.g. up to date, arrears, collector agent, legal action, judgement</small>	Amount owed \$
XYZ Finance Co	02 45645645	5555555	ARREARS	8370.00
BE MONEY	08 56756756	6666666	ARREARS	3571.40
BANKNORTH	03 67867867	7777777	ARREARS	8246.92
ABC BANK	07 34534534	1111111	ARREARS	0
BANK OF TIMBUCKTOO	03 78978978	9999999	LEGAL ACTION	11150.67
D & E SAVINGS AND LOANS	03 23423423	2222222	UP TO DATE	3590.00
MR REDS RENTALS	02 12312312	3333333	UP TO DATE	161.63
Total amount of unsecured debt				\$ 35,090.62

8.1 Debtors must also provide details of secured debts at Part D, item 12 of the statement of affairs.