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Ms Alix Gallo
The Manager
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Corporations and Capital Markets Division
The Treasury
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PARKES ACT 2600

Email: insolvency@treasury.gov.au

Dear Ms Gallo,

Exposure Draft Corporations Amendment (Phoenixing and Other Measures) Bill 2012

The Australian Institute of Company Directors welcomes the opportunity to comment on the exposure draft of the Corporations Amendment (Phoenixing and Other Measures) Bill 2012 (Exposure Draft).

The Australian Institute of Company Directors is the second largest member-based director association worldwide, with over 30,000 individual members from a wide range of corporations: publicly-listed companies, private companies, not-for-profit organisations, charities, and government and semi-government bodies. As the principal professional body representing a diverse membership of directors, we offer world class education services and provide a broad-based director perspective to current director issues in the policy debate.

Although we welcome the opportunity to comment, we would like to express our concern at the now annual practice of the Government and Treasury releasing numerous drafts of legislation in the week prior to Christmas with responses due in a compressed time frame that spans the traditional holiday period.

The government has been considering the issue of phoenix activity since at least 2009 and therefore there is no compelling reason as to why a short 5 week consultation over the Christmas/New Year period is necessary. We have responded to the request for comments in the time frame proposed simply because we are committed to ensuring that legislation is well formulated and properly based. We are strongly of the view, however, that consultation conducted in this manner falls well below good practice and is not conducive to effective engagement with the business community or reliable outcomes.

On the issue of fraudulent phoenix activity, the Australian Institute of Company Directors supports effective efforts to reduce the practice.[1] We share the Government's view that fraudulent phoenix activity is an abuse of the corporate form and the privilege of limited liability and therefore we agree in principle with the objectives of the Exposure Draft. We are however, eager to ensure that measures adopted to curtail the activities of those involved in fraudulent phoenix activity, do not unnecessarily increase the compliance burden for the vast majority of Australia's directors who govern their companies with integrity. We are also keen to ensure that the powers given to ASIC to regulate conduct that includes suspected phoenix activity are valid and appropriate.

1. Summary

In summary, the Australian Institute of Company Directors key comments are as follows:

(a) Treasury should give careful consideration as to whether providing ASIC with the power to order a winding up of a company is an exercise of judicial power. If upon its proper construction, section 489F of the Exposure Draft confers a judicial power upon ASIC it will be invalid, given that judicial powers can only be exercised by a Chapter III court under the Constitution;

(b) The current drafting of section 489H(3) regarding ASIC's power to fill a vacancy in the office of a liquidator is ambiguous;

(c) ASIC's increased powers in the Act are not confined to circumstances where fraudulent phoenix activity is suspected and apply more broadly. If the purpose of particular amendments is to address phoenix behaviour then ASIC's power should be triggered *only* when phoenix behaviour is suspected and the legislation should unequivocally reflect this purpose; and

(d) If the notification requirements currently set out in the Corporations Act are to be replaced with a regulation making power, the 'prescribed manner' should in no way diminish the ability of creditors, members and other interested persons to have notice of a corporate winding up.

These issues are discussed in more detail below.

2. Detailed consideration should be given as to the whether the power of ASIC to wind up companies is constitutionally valid

Pursuant to the Exposure Draft, ASIC would be able to order the winding up a company in four circumstances, in summary these are where:

(a) a company's response to a return of particulars is 6 months late, the company has not lodged documents under the Act for 18 months and ASIC believes the company is not carrying on a business;

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[1] See for example: Submission to House Standing Committee on Economics on *Tax Laws Amendment* 2011 (2011 Measures No.8) Bill 2011 (26 October 2011); Submission to Treasury in response to *Options Paper: A Modernisation and Harmonisation of the Regulatory Framework Applying to Insolvency Practitioners* (29 July 2011) and Submission to Treasury: *Treasury Proposals Paper, Action against fraudulent phoenix activity* (22 December 2009) available at www.companydirectors.com.au

(b) the review fee (the annual fee paid by companies usually on the anniversary of their registration date) has not been paid in full at least 12 months after the due date for payment;

(c) ASIC has reinstated the registration of the company under 601AH(1); and

(d) the company is not carrying on a business and ASIC gives the company and directors 28 days notice before making the order.

We note that section 489F(1) of the Exposure Draft specifically provides that "ASIC may order the winding up of a company." While ASIC currently has the power to de-register companies on essentially the same criteria as that proposed in section 489F of the Exposure Draft, the deregistration of a company is not the same as the making of a winding up order. Currently the Corporations Act requires ASIC to apply to a Court,[2] to seek an order that a company be wound up.[3]

Although we have not conducted a detailed analysis of this issue, we question whether the proposed section 489F confers upon ASIC a function or power pertaining exclusively to the judicial power of the Commonwealth. If, upon its proper construction the legislation does confer a judicial power upon ASIC, then it would be invalid, ASIC not being one of the courts identified in chapter III of the Constitution.[4]

While recent High Court decisions have held that disqualification orders and certain disciplinary proceedings have not involved the exercise of judicial power by the federal executive and were valid[5], we query whether the High Court would take this view in regard to the ability of ASIC to order the winding up of a company. Historically, similar powers in bankruptcy and sequestration have been considered judicial powers.[6] Further, the Commonwealth parliament through the Corporations Act has already conferred the power to wind up a company on Courts.

The Explanatory Notes to the Exposure Draft refer to the right of appeal under section 1317B of the Corporations Act, which may suggest that the order made by ASIC is not intended to be conclusive and therefore not like a judicial power. Further, the Explanatory Notes suggest that the Exposure draft confers an "administrative power" on ASIC to order the winding up of a company. Despite this, no other discussion is provided as to the basis for Treasury's view that the power is merely administrative.

It may be that Treasury has sought the advice of the Attorney General in regard to whether the separation of powers doctrine is contravened by the proposed conferral of power on ASIC. If this has not occurred, we recommend that Treasury seek the advice of the Attorney General as to whether section 489F potentially confers upon ASIC a judicial power (rather than an administrative one) which may render the provision invalid.

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[2] Court is defined in section 58AA of the Corporations Act 2011 (C'th) and the definition includes the Federal Court and the Supreme Court of a State or Territory.
[3] See for example, s. 462(2) and s.464 of the Corporations Act (2001)(C'th). The Act gives the Court a range of powers to make winding up orders and related orders. As examples see s. 459A, s.459T(2), s.461, s. 467, s. 467B, s. 482, s.472 and s.490 of the Act.
[4] See *Visnic v ASIC* (2007) 231 CLR 381 at 385.
[5] See for example, *Visnic v ASIC* (2007) 231 CLR 381 and *Albarran v Members of the Companies Auditors and Liquidators Disciplinary Board & Anor; Gould v Magarey and Others* (2007) 231 CLR 350
[6] See for example, *R v Davison* (1954) 90 CLR 353

3. ASIC's power to fill a vacancy in the office of a liquidator is ambiguous

Section 489H(3) of the Bill gives ASIC the power to appoint a liquidator. Section 489H(3) provides that if there is "a vacancy in the office of a liquidator appointed by ASIC it is to be filled by ASIC." It is not clear from this drafting whether the proposed provision is intended to mean that:

(a) ASIC will take responsibility for filling the vacancy, (i.e. by identifying an alternative liquidator and appointing them); or

(b) ASIC will fill the vacancy itself by assuming the role of the liquidator and conducting the liquidation.

Although we expect that the interpretation in sub-paragraph (a) is intended, if the interpretation in sub-paragraph (b) is accepted, ASIC would be in a position where it orders the winding up, appoints itself as liquidator and conducts the liquidation. Such an outcome would raise concerns about the appropriateness and breadth of the powers given to ASIC and would further agitate the questions around the separation of powers doctrine raised in paragraph 2 above. To avoid the potential for ambiguity we recommend that section 489H(3) be re-drafted.

4. ASIC's increased powers in the Bill to target phoenix activity are not confined to circumstances where phoenix activity is suspected

We note that the Exposure Draft forms part of the Government's initiatives to tackle fraudulent phoenix activity. Despite this, the provisions marked as providing mechanisms to address possible fraudulent phoenix activity are not in fact limited to circumstances where fraudulent phoenix activity is suspected. For example, pursuant to section 601AH of the Act ASIC has the power to "reinstate the registration of a company if it satisfied that the company should not have been deregistered", the Exposure Draft then provides that ASIC may order the winding up a company if "ASIC has reinstated the registration of the company under subsection 601AH(1)." These provisions apply regardless of whether fraudulent phoenix activity is suspected and give ASIC broad powers to reinstate companies and then order a winding up regardless of whether the company has previously been deregistered appropriately.

Given that phoenix activity is often characterised as "the deliberate, systematic and sometimes cyclic liquidation of related corporate trading entities"[7] we anticipate that ASIC will be more likely to use its powers to wind up companies to deal with abandoned companies rather than in instances of phoenix activity (where operators commonly put their companies into liquidation).

While we have no objection to the underlying purpose of the Bill which is to target phoenix activity and protect workers entitlements, we caution Treasury against broadening ASIC's power to 'target phoenix activity' when the powers are not confined to suspected instances of phoenix activity and apply much more broadly. If the purpose of particular amendments is to address phoenix behaviour then ASIC's power should be triggered *only* when phoenix behaviour is suspected and the legislation should unequivocally reflect this purpose.

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[7] See for example, the "*Action against fraudulent phoenix activity*" Proposals Paper November 2009 at 1.

5. The 'prescribed manner' of notification should not diminish the current ability of interested parties to be notified as to a winding up

Part 2 of the Exposure Draft proposes to repeal a number of current notification requirements in the Act[8] and to replace them with a requirement that notices be published in 'the prescribed manner.' The prescribed manner would be set out in the regulations, although no indication is provided as to the likely content of the requirements that will be prescribed.

While we have no objection to a regulation making power for notifications per se, we are of the view that it is important for creditors, members and other interested parties to have timely notification of applications, appointments, resolutions and meetings that may impact their interests. For this reason, we recommend that the 'prescribed manner' set out in the regulations does not in any way diminish the current ability of relevant parties in an administration or liquidation to obtain notification of winding up issues in a timely and accessible manner.

If you would like to discuss any aspect of our views please contact me on (02) 8248 6600.

Yours sincerely,

John H C Colvin
CEO & Managing Director

[8] These notifications include the appointment of an administrator, winding up resolutions, applications for winding up and convening of creditors meetings, as examples.