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Dear Sir/ Madam

Improving bankruptcy and insolvency laws

CPA Australia represents the diverse interests of more than 155,000 members in 118 countries. Our vision is to make CPA Australia the global accountancy designation for strategic business leaders. We make this submission on behalf of our members and in the broader public interest.

CPA Australia has had a long term interest in this area of law reform having made a submission to the 2015 Productivity Commission inquiry into Business Set-up, Transfer and Closure. We have also previously been a member of related consultations such as the Insolvency Law Advisory Group, which oversaw the significant 2007 reforms to Chapter 5 (External Administration) of the Corporations Act 2001.

Before addressing the Proposal Paper questions, we wish to make some initial cautionary observations concerning the process and rationale of the proposed bankruptcy and insolvency law reforms, acknowledging that the reforms are well entrenched in the Government's innovation and science agenda.

Australia has benefited from a cautious though deliberately well targeted approach to bankruptcy and insolvency law reform seeking to balance a range of interests. The reality is that there is no perfect solution to the circumstance of a debtor's inability to pay creditors and there is invariable friction between the legal realities of unfulfilled contractual and other obligations, and the social and economic consequence of the event of insolvency. If changes are to be made it is incumbent on Government to both fully explore the possibility of unintended consequences and show a rigorous basis for confidence that the reforms will deliver the positive outcomes promised.

The proposed corporate law reforms are measured and address longstanding concerns about the discouraging of a strong business turnaround and risk taking culture. Nevertheless, this predominantly economic policy objective should not ignore other aims of these laws including creditor protection, weeding out the dishonest and incompetent, and supporting market transparency.

A further central aspect of the reforms is reducing the bankruptcy period to one year. CPA Australia is concerned that without other complementary policy initiatives the Proposal Paper's assertion of promoting an entrepreneurial culture is illusory. Nor, do the characteristics of those individuals who

find themselves in this often tragic circumstance support the asserted economic benefits. The Australian Financial and Security Authority (AFSA) maintains a comprehensive set of bankruptcy statistics. These show that in 2013-14 only 19 per cent of personal bankruptcies were because of business related reasons. Prominent in the non-business reasons are factors such as excessive use of credit, with the most significant cause being unemployment. Among causes of business-related personal bankruptcies, economic conditions dominate. AFSA's statistics also identify the occupation of individuals who have succumbed to bankruptcy. Overwhelmingly these occur amongst clerical and administrative workers, sales assistants, road drivers and labourers. The statistics on the age of insolvent debtors is also insightful, the most common in 2008 being 37 years, though by 2014, risen to 43 years. These characteristics are not what we would think as typical of innovators and entrepreneurs.

We provide our response to the Proposals Paper Queries below.

Query 1.1
The government seeks views from the public on whether the criteria for lodging an objection and the standard of evidence to support an objection should be changed to facilitate a trustee's ability to object to discharge.
CPA Australia believes that this matter should be subject to careful monitoring. The grounds of objection listed in s 149D of the Bankruptcy Act 1966 are comprehensive and the s 149C(2) protection against notice invalidity safeguards the trustee's powers. The shortening of the discharge period may have unintended consequence of a significant rise in the number of objections to discharge, and within these, shortcomings in the detail of stated grounds of objection.

Query 1.2.1a
The Government seeks views from the public on whether particular obligations on a bankrupt should continue even after a bankrupt is discharged.
CPA Australia believes it essential that the post discharge assistance obligations of s 152 and the exceptions from release applied under s 153(2) continue to be available and vigorously applied. Consideration should be given to the adequacy and practicalities of the deterrent impact of the imprisonment penalty (6 months) currently available for applying to errant discharged bankrupts under s 152.

Query 1.2.1b
The government seeks views from the public on what incentives and mechanisms should be in place to ensure compliance with obligations after discharge.
Additional to our comments above, the central safeguard of compelling post discharge income contributions is essential to the integrity of the bankruptcy system. Aside from drafting challenges within the various sections of Division 4B (Contribution by bankrupt and recovery of property), specific attention needs to be paid to the adaptability and responsiveness of the injunction powers under s 139ZIJ to these new circumstances.

Query 1.3.1
The government seeks views from the public on whether it is appropriate to reduce the retention period for personal insolvency information in credit reports.
The stated intention in reforming s 149(2) is to hasten the speed with which innovators and would-be entrepreneurs can re-establish themselves in their budding ventures. There is no basis for the s 269 restriction on obtaining credit not to align with this alteration to discharge period. Credit provider protection is a separate matter and CPA Australia sees no basis for reducing the retention period for personal insolvency information.

1.3.2 Overseas travel
Proposal 1.3.2
The Government proposes to reduce the overseas travel restriction to one year, subject to any extension for misconduct.
As with our response immediately above, consistency warrants overseas travel restrictions likewise being aligned to the discharge period, so long as trustee actions against misconduct are readily and efficiently able to be applied.

1.3.3 Licences and industry associations
Proposal 1.3.3
The Government proposes to consult with relevant industry and licensing associations with a view to aligning restrictions with the reduced period of bankruptcy, where appropriate.
CPA Australia strongly urges Treasury, and indeed AFSA, to liaise and exhaustively explore the implications of the proposed alignment in the specific context of our members. Member insolvency is identified as a basis for penalty in our Constitution under Professional Conduct. You will appreciate that the terms of our Professional Conduct are structured foremost with the view to protecting the public interest and trust in the accounting profession. These matters are of great importance and should transcend objectives of encouraging entrepreneurial behaviour. Similarly, it should be appreciated that the requirement of due process within our professional conduct investigation and discipline arrangements can be protracted.

2.2 Safe Harbour Model A – Proposal 2.2
Query 2.2
Subject to the further information on the proposal set out in the sections below, the Government seeks views from the public on whether this proposal [Proposal 2.2] provides an appropriate safe harbour for directors.

- In relation to "based on advise provided", we query whether it may be appropriate to cross-reference to s 189 (Reliance on information or advise provided by others), and indeed, whether or not the basis of reliance should be more or less strict than the general statutory rule. Additionally, any overlap or conflict with the existing s 588H(3) defence will need to be addressed.
- The proposal states "The defence would apply where the company appoints a restructuring adviser who: (b) is and remains of the opinion - - - ." We query here whether "opinion" shifts the onus or burden which correctly sits with directors and their judgment. Furthermore, it may be that this apparent shift in emphasis to the role of the restructuring adviser is at odds with the foregoing draft introduction, which emphasises a reliance relationship.
- The final sentence of Proposal 2.2 makes reference to "powers" and "duties" of the restructuring adviser. CPA Australia believes it incumbent on Treasury that both attributes be defined and explained in statute, or at a minimum, within the Explanatory Memorandum. Determining these attributes should precede any specifying of qualifications and professional membership of those individuals who might be appointed as restructuring advisers.

2.2.1 The restructuring adviser
Query 2.2.1a
The Government seeks views from the public on what qualifications and experience directors should take into account when appointing a restructuring adviser and whether should be set out in regulatory guidance by the Australian Securities and Investments Commission, or in the regulations.

Query 2.2.1b
The Government seeks views from the public on which organisations, if any, should be approved to provide accreditation to restructuring advisers if such approval is incorporated in the measure.

Outcomes in relation to these two questions will, CPA Australia believes, depend on how prescriptive Government wishes to be in recognising this novel form of corporate adviser. Some level of formal recognition is necessary given that the restructuring adviser is being worked into the statutory wording of a safe harbour for directors. A very minimalist approach seems undesirable, yet the more the statutory recognition is seen to take on the guise of detailed prescription, the more questions arise. Nevertheless, some guidance can be drawn from the current 'dual' approach to registered liquidators taken under s 1282 of the Corporations Act and ASIC's regulatory guide RG 186 – *External administration: Liquidator registration.* Section 1282(2) [Requirements for granting application] is not overly expansive, yet identifies three attributes which ought to be considered for adaptation to the restructuring adviser context: education attainment, experience and being a fit and proper person Mention here of s 1282 of course begs the question of whether restructuring advisers should be subject to a scheme of registration. Without necessarily advocating a highly formalised approach there are significant overriding issues of market integrity and protection of a wide constituency of interests. The education requirements specified in s 1282(2)(a)(ii) likewise appear highly pertinent in that possible entrepreneurial enthusiasm will need to be tempered by a high level of awareness of the general and specific legal issues associated with the operation of companies, particularly when under financial stress. While sympathetic to concerns about market concentration, CPA Australia believes it may well be that the particular needs underlying the proposed reforms are best served by formal recognition of this particular form of professional service within existing insolvency services. As such, we are particularly concerned about the potential risk of a proliferation of businesses advising actions which are either illegal or highly questionable. By no means a watertight panacea, there are significant safeguards within a co-regulatory environment where practitioners are subject to a code of professional conduct and independent oversight in the form of practice quality reviews and discipline for breach of professional conduct.

Turning now to RG 186. Guidance such as this from ASIC serves the important purpose of expanding upon the applied aspects of statute. CPA Australia does not believe it possible at this juncture to suggest what might be the detail within a regulatory guidance for restructuring advisers. We do however wish to point to one of the significant preamble paragraphs within RG 186. There it is stated: "Our [ASIC's] approach to this guide has been influenced by the fact that registered liquidators act in fiduciary capacity, often have total management control of the affairs, money and other property of a body corporate, and in some cases, are officers of the court." Statements such as these are vital in setting both the context and boundaries of regulatory oversight, and as such, inform market participants as to the expectations expressed in the law.

Query 2.2.1c
Is this an appropriate method of determining viability?

Query 2.2.1d
What factors should the restructuring adviser take into account in determining viability? Should these be set out in regulation, or left to the discretion of the adviser?
CPA Australia provides a combined response to queries 2.2.1c and 2.2.1d:

- "be returned to solvency" – it is unclear whether this statement infers that a company under consideration is insolvent, rather than suspecting that the company may become insolvent, and if so, is there a need to consider creditor moratorium arrangement?
- "within a reasonable period of time" may suggest an open-endedness which should be avoided. Indeterminate or delayed resolution would be counterproductive to the underlying economic justification for the proposed changes.
- More broadly, "viability" is likely to be very firm specific and it will be difficult to specify in prescriptive terms characteristics and indicia. Similarly, there will be practical challenges in unbundling firm specific features from wider economic transformation that will often come into play. Nevertheless, CPA Australia believes it most important that both directors and the restructuring adviser should remain particularly mindful of solvency declaration or resolution requirements respectively under s 295(4)(c) and s 347A (along, where applicable, with

more specific listed entity requirements such as 295A[1]), and associated with this, the underlying expectation of being able to pay debts as and when they become due and payable.

- Similarly, during the course of the viability assessment, and any consequent restructure, attention will need to be paid to the implications for disclosure under Australian Accounting Standards AASB 101 Presentation of Financial Statements.[2] In particular, para. 25 imposes a going concern assessment, requiring "when management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties." A proposed restructure would seem certain to be considered in the going concern basis of financial statement preparation and any need for disclosure of uncertainties.
- To conclude our response on these particular matters, CPA Australia is of the firm view that the factors relevant to determining viability should not be left entirely to the discretion of the restructuring adviser. Market transparency, investor and creditor confidence, and regulatory integrity all warrant development of suitable regulatory guidance, though a relatively non-prescriptive principle-based approach may be suitable.

Query 2.2.1e

The Government seeks views from the public on whether these are appropriate protections and obligations for the restructuring adviser, and what other protections and obligations the law should provide for?

- The good faith and best interests of the company requirements are accepted norms both in common law and statute (s 181) and would be highly appropriate expectations to place on the restructuring adviser. Yet, whilst "powers" and "duties" remain undefined, or at best ill-defined, there is presently a risk of indeterminacy of how this will apply in practice.
- We urge caution about intended exclusion from civil liability and believe this should be more fully explored in the context of current approaches to economic torts and expectations of reasonable foreseeability of harm. Further complexity may arise if the claimant is the company itself and in circumstances where the directors action are alleged to be reliant upon the advice of the restructuring adviser.
- The proposed prohibition of subsequent insolvency appointments is sound and essential to the actuality and appearance of independence, compelling uncompromised attention to the restructuring appointment itself.
- More generally, in any significant matter affecting the interests of parties dealing with and through a corporate entity, matters of independence will be paramount. With the structuring adviser's stated role "to form an opinion", does this cloud the restructuring advise itself? In other words, can the opinion be truly independent when the restructuring adviser has a potential commercial interest in the outcome?
- The intention of protecting the restructuring adviser through deliberate exclusion from the s 9 recognition of de facto and shadow director is acknowledged. Given this proposal, we urge for consistency, consideration of the exclusion of the restructuring adviser from the s 9 definition of *officer*. Without offering a firm conclusion, this may add emphasis to the advisory role under which the directors retain control and avoid confusion, say for example, in the operation of Part 2B.2 (Assumptions people dealing with companies are entitled to make).

[1] Declarations in relation to listed entity's financial statements by chief executive officer and chief financial officer.

[2] Accounting standards are given effect through legislative instrument (s 334) and are required to be complied with by all disclosing entities, all public companies, all large proprietary companies and all registered schemes through effect of s 296.

2.2.2 Other features of safe harbour
Query 2.2.2a
Do you agree with this approach?

- **Directors to remain subject to all other obligations that the law provides**
  CPA Australia agrees with this measure. Any discussion in Explanatory Memoranda, or similar materials, should, aside from the unreasonable director related transactions provisions, make direct reference to the general duties contained in Division 1 of Part 2D.1 – Duties and powers. Indeed, it may be beneficial to adapt from the type of wording used in s 230 (General duties still apply) of Part 2E.2 – Related parties and financial benefits.
- **Civil claims against a director which accrued during the safe harbour period**
  CPA Australia agrees but urges appropriate consideration be given to potential impact on the operation and funding of the General Employment Entitlements & Redundancy Scheme (GEERS).
- **Disregards of safe harbour defence in calculating any reach-back period for director related party transactions**
  This is certainly a highly sound in principle, however our concern is that if the duration of the safe harbour is protracted this may cause uncertainty and dispute in determining the type of preference or transaction to which the clawback mechanism in s 588FE (Voidable transactions) is applied.

Query 2.2.2b
Do you agree with our approach to disclosure?
CPA Australia acknowledges the need for a degree of privacy as informal workout options are explored, and thus, the type of notice in public documents required by s 450E of Part 5.3A would be both counterproductive and burdensome. The Proposal Paper's inferred reliance on the continuous disclosure obligations as a means of protecting investors and the wider market is, of course, limited to listed disclosing entities (Chapter 6CA). Given the likelihood of the availing of safe harbour relief by both listed and non-listed companies, the need for disclosure ought therefore, to be monitored as part of the early rollout of any informal workout scheme.

2.2.3 Where safe harbour is not available
Query 2.2.3
The Government seeks views from the public on what other circumstances should the safe harbour defence not be available.
What is presented here in the Proposals Paper is a sensible and comprehensive list of exclusions from the availing of the safe harbour. The discussion however raises a minor concern which appears not to be addressed in the Proposals Paper. Presently, members have specific rights and remedies under Chapter 2F of the Corporation Act 2001. Pursuit of these rights and remedies can, through Court order, result in a range of regulation or alteration to the company's affairs. CPA Australia believes that there would be merit in an appropriately placed clear statement that the development of the restructuring proposal, and its accompanying safe harbour, in no way undermines or interferes with members' rights and remedies.

2.3 Safe Harbour Model B
Query 2.3
The Government seeks feedback on the merits and drawbacks of this [alternative] model of safe harbour
This alternative has, in CPA Australia's view, the distinct advantage of overcoming uncertainty as to defining the scope of a restructuring adviser's role, powers and duties, and accordingly, the challenge in drafting of any defence within s 588H. Additional to the Discussion Paper's reference to the Explanatory Memorandum 'discussing more fully the indicia of both "reasonable steps" and "reasonable time"', both "honest - - - belief" (in (b)) and "serious loss" (in (c)), should also be the subject of more detailed description and explanation.

3 Ipso facto clauses
3.2 The Ipso Facto model
Query 3.2.a
Are there other specific instances where the operation of the ipso facto clauses should be void. For example by prohibiting the acceleration of payments or the imposition of new arrangements for payment, or a requirement to provide additional security for credit.
CPA Australia regards these additional complementary measures as having merit. These would give certainty to contract negotiations and performance, and ameliorate against risk of conduct that would otherwise potentially be unconscionable.

Query 3.2.b
Are there any other circumstances to which a moratorium on the operation of ipso facto clauses should also be extended?
The circumstances as listed appear complete and comprehensive.

3.2.1 Anti-avoidance
Query 3.2.1
Does this constitute an adequate anti-avoidance mechanism?
Yes, and should effectively work against any allegation that the parties have contracted-out of the ipso facto prohibition.

3.2.2 Exclusions
Query 3.2.2
What contracts or classes of contracts should be specifically excluded from the operation of the provision?
No further comment, other than to support the proposed exclusions.

3.2.3 Appeal
Query 3.2.3
Do you consider this safeguard necessary and appropriate? If not, what mechanism, if any, would be appropriate?
Yes, this safeguard is essential.

If you have any questions regarding this submission, please do not hesitate to contact our Policy Adviser ESG, Dr John Purcell FCPA on +61 3 9606 9826 or at john.purcell@cpaaustralia.com.au.

Yours faithfully

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