8 March 2013

The Manager
Corporate Governance and Reporting Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent
Parkes ACT 2600

Attention: Mr Aaron Jenkinson
Email: insolvency@treasury.gov.au

Dear Mr Jenkinson

Insolvency Law Reform Bill 2013- Exposure Draft

McGrathNicol is a national practice of 31 partners, 19 of whom are registered liquidators; in addition, two of our senior employees are also registered liquidators. The majority of our registered liquidators are members of the Insolvency Practitioners Association of Australia (IPA). Our insolvency practice is confined to corporate engagements typically the larger, more complex matters; we do not practise in bankruptcy.

We welcome the government's interest in improving the legislative framework for the important work undertaken by insolvency practitioners in contributing to the stability and effectiveness of Australia's economy.

We also welcome the opportunity to make a submission in regard to the proposed amendments to the *Corporations Act 2001* (the Act) detailed in the Insolvency Law Reform Bill 2013.

Our detailed comments are set out in the attachment to this letter. Our comments address only those aspects of the proposals where we wish to point out practical implications, concerns regarding the effectiveness of the law reform proposals or the manner in which they may be implemented. We have confined our comments to the area of corporate insolvency as our firm does not practice in personal insolvency.

By way of highlighting the themes which underlie our detailed comments we make the following comments in regard to the overall direction and scope of the proposed amendments:

Harmonisation

In general terms we have no objection to the harmonisation of the corporate and personal insolvency regimes and recognise that this may have potential advantages for regulators, creditors and practitioners who conduct both corporate and personal insolvency practices.

However, a number of our detailed submissions concern the results of the attempt to harmonise the regimes without due regard to the significant and substantive differences between corporate and personal insolvency.

Insolvent companies typically involve a far greater number and value of creditors than personal insolvencies and are far more likely to be trading enterprises and employers. The harmonisation approach appears to have taken the view that processes and requirements that work well in bankruptcy can be applied, without modification, to corporate insolvency. There are certainly aspects

Level 8, IBM Centre, 60 City Road, Southbank VIC 3006, Australia GPO Box 9986, Melbourne VIC 3001 T +61 3 9038 3100 F +61 3 9038 3199
McGrathNicol Partnership ABN 41 945 982 761. Liability limited by a scheme approved under *Professional Standards Legislation* **mcgrathnicol.com**

in which this premise holds, but there are several where it does not and, in our view, harmonisation in these aspects will unnecessarily add cost and confusion.

In the absence of detail regarding any proposed consequential changes in the law in relation to receiverships, aspects of the proposed Uniform Insolvency Practice Rules will have the effect of undermining the harmonisation that presently exists between the different types of corporate insolvency. We submit that this outcome is potentially likely to cause greater confusion among creditors than the mischief that is sought to be remedied by the harmonisation of the corporate and personal insolvency regimes.

Complexity

Taken in isolation, most, if not all, of the changes proposed appear reasonable and well targeted on issues which have been identified, through the Senate Inquiry and subsequent consultations, as in need of reform. However, in our view, collectively the amendments risk excessive layering of controls and processes and result in undue complexity.

We submit that there is a need to consider the collective impact of the amendments and consider opportunities to simplify and rely on over-arching controls or common mechanisms to achieve the core objectives, and minimise the cost burden of compliance which is ultimately borne by creditors.

Insolvency Practitioners Association ("IPA")

In the course of reviewing the proposed amendments and developing our submission we have liaised with the IPA. We support the general comments raised by the IPA in its submission insofar as they concern corporate insolvency law and practice.

Regulations and consequential amendments

As you would know, the proposed Uniform Insolvency Practice Rules point towards a great deal of the detail being dealt with by regulations which have not been released for comment. This fetters our ability to fully understand the proposals and provide constructive input in regard to how the regulations are likely to play out in practice.

In addition, it would seem that consequential amendments will be required to the Act in order to implement the new Uniform Insolvency Practice Rules. Again in the absence of the detail in this regard we are unable to provide constructive feedback into the process to assist in ensuring there are no unintended consequence in practice.

We would welcome the opportunity for consultation on these aspects of the law reform in due course.

If you have any queries or comments in regard to our submission, please contact me or Rosemary Winser on 08 8468 3701.

Yours faithfully

Robyn McKern
Partner, CEO

Detailed comments and submissions in relation to
Schedule 1- Uniform Insolvency Practice Rules

Part 2 – Registration and Discipline of Insolvency Practitioners

Section	McGrathNicol commentary
Division 8 – Registering Liquidators 8-10 – 8-85	The timeframe for obtaining registration is significantly longer under the proposed amendments than the current regime administered by ASIC. Six months plus 45 business days is an undue gap between the submission of an application and registration based on our experience that the current average timeframe is approximately 8 weeks. We submit that as registration is a critical business tool a period of 7.5 months represents an excessive delay and undermines the policy goal of encouraging a robust and competitive insolvency market and also opens up the risk that the data upon which the application is assessed falls out of date during the assessment period. As we have raised in previous submissions in relation to reform proposals, the new registration process must entail recognition of skills obtained through undertaking restructuring, receiverships and advisory work such as independent business reviews. These skills are directly relevant to voluntary administrations, deeds of company arrangements and liquidations and experience gained in these matters equips practitioners to search for solutions which seek to preserve economic value and employment.
Division 12 - Annual Liquidator returns 12-5	It would be useful to understand the expected format of the approved form. On the assumption that it will cover similar content to the triennial registration renewal form, we suggest that the forms be combined with each third annual return serving as the registration renewal to avoid unnecessary duplication.
Division 16 – Disciplinary and other action 16-15 Registered liquidator to correct inaccuracies	We submit that the window for ASIC's review/amendment of lodged documents be limited to 12 months, so documents are not indefinitely subject to review/amendment.
16-55 ASIC may convene a [disciplinary] committee	Nominees to the committee should be persons who are no longer practising (in insolvency), to avoid the potential for conflict of interest. If this is not feasible, the liquidator under review by the committee must able to object to nominees on the basis of conflict, such objections to be subject to the reasonable review of the IPA and ASIC (noting that 18-10(3) indicates that the Minister's power to appoint a member will most likely be delegated to ASIC).

Part 3 – General Rules Relating to External Administration

Section	McGrathNicol commentary
Division 22 – Remuneration and other benefits received by EAs 22-10 EA's remuneration	The default remuneration amount of $5500 appears to represent a minimum fee for a first appointed external administrator (EA). This part of the amendment implies that a second appointed EA has no entitlement to the default remuneration amount and this may act as a disincentive for a proposed replacement (second) administrator to consent to act. The amount should be provided for expressly inclusive or exclusive of GST.
22-15 Remuneration determinations	The removal of the current power of a Committee of Inspection (CoI) (and presumably a creditors' committee in a VA or DoCA), to determine the remuneration of an EA has potential to create a very cumbersome process for dealing with remuneration determinations, especially on appointments with large numbers and classes of creditors. Our experience is that committees provide a more workable body than a general meeting for the EA to communicate with, and meetings may be convened much more readily and cost effectively. As committee members will generally be bound by a confidentiality deed, the EA is able to provide a more complete account of commercially sensitive matters to the committee. Committee members are likely to have more insight into the EA's dealings than the general body of creditors and are therefore better placed to assess remuneration requests. Under the amendments, if creditors do not delegate to the committee the power to determine the EA's remuneration, the remuneration determination process is likely to incur increased costs. We submit that the automatic power of a duly elected committee to fix the EA's remuneration should remain.
22-35 EAs must disclosure of employment etc of related entities	In practice, very many practitioners operate their businesses through structures which involve service entities which provide staff to the practitioner. Whilst generally we are supportive of prior disclosure of the proposed employment or engagement of a related entity, it would be wholly impractical and of little utility to make disclosure of this sort of operating structure in advance. Accordingly, there should be an exception for the EA's firm and any service entity employing staff, alternatively the section should be drafted to better target the mischief which it seeks to address.

Section	McGrathNicol commentary
22-45 EAs must not accept extra benefits etc	This amendment appears broad and absent the regulations which may better define "extra benefits" it is difficult to comment on an informed basis. We would be concerned if, in the final drafting, this clause prohibited: + payments in advance or indemnities provided by third parties as security for costs or remuneration to be incurred. + reasonable entertainment or technical presentations provided by service providers (eg law firms, insurance brokers)
22-50 EAs must not give up remuneration	Clarification of this proposed amendment is required as it is unclear what 'give up' means in this context. We are concerned that it is open to the interpretation that the very common form of practice, being a profit-sharing partnership where the EA's remuneration is paid to that partnership, might offend this proposed provision.
22-55 EAs must not purchase any assets of the company	We submit that this restriction should be modified in line with, the COPP and APES 330, which allow the EA, his partners, his associates, his staff and their close or immediate family to acquire assets from a retail operation under administration of the EA, where those assets are available to the general public for sale and where no special treatment or preference over and above that granted to the public is given. Absent this modification, there is high risk that this amendment could be unintentionally breached by a family member of the EA of his/her staff who are unaware of the appointment.
Division 24 – Funds handling 24-10 Opening and paying money into administration account	The proposed amendment to open a single bank account within 5 business days of appointment appears to be required regardless of whether there are, or are likely to be, funds to bank in relation to the external administration. As most banks will levy account maintenance fees whether or not there are any transactions in the account, it would be an unnecessary burden for the EA to have to cover these costs personally. We also see no basis for the requirement that a single account be opened – it may well be more appropriate from a logistics, risk management and investment return perspective to open multiple accounts. We submit that the requirement be amended to require a bank account be opened for the external administration within 5 business days of <u>becoming aware</u> that funds are likely to be received by the EA in relation to the company. In relation to the paying in of monies, there should also be a recognised exemption where it would prejudice a recovery by banking a cheque tendered in offer of settlement of a dispute.

Section	McGrathNicol commentary
24-15 Consequences for failure to pay money into administration account	In the context of corporate insolvency, $50 is a very low threshold amount, we submit $250 would be more appropriate. Payment of penalty interest to the Commonwealth provides no compensation to the stakeholders in the administration estate for any loss of interest earned on the funds had they been banked earlier and we query the value of this provision. A criminal penalty seems extreme as a remedy for a breach of this provision.
24-20 Paying money out of administration account	We advise that for high volume matters the use of the electronic signature of the EA on bulk cheque payments (eg, dividend payments to creditors) is common and efficient. We would be concerned if the language of this provision precluded this practice.
24-35 Receipts for payments into and out of an administration account	We are opposed to the new requirement that the EA obtain a receipt for a payment made out of the administration bank account. The provision contains is no threshold limit for the amount of a payment requiring a receipt and no exceptions. Whilst the requirement is limited to cases where it is "practicable" to obtain the receipt – does this mean a receipt must be sought in all cases but can only be considered impracticable if the recipient refuses to provide the receipt? We submit that this amendment is impractical and burdensome and we question its utility in the present corporate business environment. For example, in trade-on appointments, the request for receipts for payments made to employees and suppliers is likely to be poorly received, as they would not normally have provided such receipts in the normal course of dealing with the entity during the pre-appointment period. Furthermore, the requirement for the EA to seek receipts will unnecessarily increase the costs of administering the estate, which is likely to be unwelcome by the stakeholders.
24-40 Handling securities	The use of the term 'securities' here does not seem to be consistent with the definition in the Act (debentures, shares, units, interests in an MIS) and it requires clarification. A criminal penalty seems extreme as a remedy for a breach of this provision.
Division 26 - Information 26-10 Annual administration return	We have strong concerns regarding the impracticality and lack of effectiveness of this proposed amendment. In our opinion it will diminish the quality of information available for creditors in that: + the frequency with which information is available is halved; + timing issues will mean that there may be lengthy delays in disclosing any substantive information about the transactions in an external administration. For example an appointment in early July

Section	McGrathNicol commentary
	will not be required to submit a report until 25 July the following year, this may be seen as a loophole capable of manipulation. + external administrations with high levels of transactions will have reports which are approximately double the current length, making them more difficult for creditors/interested parties to interpret. The result of this proposed amendment would seem to undermine, rather than promote, the stated goal of providing greater transparency around the conduct of external administrations. In addition, we are of the view that for practitioners who undertake insolvency matters exclusively, there are serious workflow consequences involved in seeking to concentrate the reporting on all matters to a 5 week period. Presently, this reporting (under the Form 524 regime) is spread throughout the year based on 6 monthly intervals from the appointment dates, which are random. This is a system which works and which provides a regular flow of information to ASIC and creditors (albeit we believe that the form and the content of the Form 524 leaves much to be desired in terms of its utility in providing useful information to both these stakeholders). We recognise that bankruptcy trustees operate under a regime akin to that proposed. However, we submit that the number of appointments held concurrently by a corporate insolvency practice and the volume of data and transactions involved in corporate insolvency compared to bankruptcy renders invalid the assumption that it is sensible to impose the bankruptcy regime on corporate insolvency practices. We would be pleased to assist in working towards a solution which better addresses the stakeholder interest in obtaining timely and useful reporting in a manner which can be reasonably accommodated by practitioners. The starting point for this is gaining clarity on the stakeholders involved and their information needs.
26-15 Books of external administration	This amendment expands the rights of creditors and members to inspect the files of an external administration well beyond the current rights in section 486. EAs should have the power to deny access to commercially confidential information and documents subject to legal professional privilege. With regard to the proposed requirement that the EA 'ensure that the books are kept in the EA's office' we suggest that this may be impractical both in cases where there is an operating business under the EA's control (where efficiency would dictate that books recording the transactions of the EA be held on site) and where there is a very significant quantum of records. As an alternative, we submit that the provisions should require the EA to maintain control, rather than physical possession, of the books as defined in 26-15. This would still enable the requirement of allowing reasonable access to creditors requesting inspection to be accommodated.

Section	McGrathNicol commentary
26-25 – 26-35 Audit of administration books- ASIC/the Court	It is unclear what level of priority is to be afforded these audit costs but we submit they should not have a priority over the EA's fees and costs. In addition, the position with regard to these expenses in the case of an assetless administration requires clarification
Division 26D – Giving Information etc to creditors and others 26-50 – 26-59	We are accepting of the principle that reasonable requests from creditors for information should be satisfied. However, it is difficult to comment on the effectiveness of this qualification until the test for reasonableness in the regulations is available for review. We submit that "reasonableness" should be a matter for the EA to determine and that, as a minimum, the EA is entitled to take into account the cost of complying, the use to which the information is anticipated to be put, commercial confidentiality and privacy concerns, the impact on the administration of complying, the funds available, the parties to whom the information is to be provided. The draft provisions are silent as to who bears the cost of providing information and to whom information must be distributed, which we regard as a deficiency. If the cost is to be borne by the administration, this goes back to a question of reasonableness of the request which may be impacted by such factors as: + the time costs of responding to the request + the costs relative to the available assets of the administration + the size of the creditor's claim relative to the overall value of creditors + whether the creditor seeking information is a related party, a potential purchaser, an ongoing supplier, or involved in litigation with the company or EA.
Division 26D - Giving Information etc to creditors and others 26-60	We recognise that giving creditors, members or committees of inspection the ability (even if limited) to replace or modify by resolution specific requirements imposed by regulations may offer practical benefits, but it would be useful to understand which regulations it is contemplated may be modified in order to determine the appropriate way to respond to this proposal. We note that the draft Bill does not: + deal with nuisance or vexatious requests + address the costs and potential delays to the progression of the administration + provide for how reports must be distributed (to all creditors or just the requesting parties?) + establish who is responsible for setting the topics the report must address The regulations will need to address these issues. Any regime proposed by the Committee should be subject to the reasonableness test as determined by the EA with ASIC as the final arbiter for what is reasonable, should this be in dispute.

Section	McGrathNicol commentary
Division 26E – Other requests for information 26-65	We query where this proposed amendment may lead. For example, does this pave the way for requests for information from DWEER under the Fair Entitlements Guarantee Act by the Commonwealth without payment? We submit that an express provision should be made providing for the party requesting this information to bear the costs of so providing.
Division 26R – EA may be compelled to comply with requests for information 26-70 – 26-80	In principle we would have no objection to this process, on the assumption that EA will not be compelled to comply with unreasonable requests; ASIC being the arbiter of "reasonableness" based on the factors which we outline above and trust will be included in the regulations.
Division 28 – Meetings 28-5 – 28-40	In general terms we are concerned that this new mechanism creates an overly complex process for convening meetings. This does not seem to be a harmonised provision as the rules applying in bankruptcy do not contain this level of complexity. We suggest that this amendment should be drafted in similar terms to the provisions dealing with the provision of information to creditors covered in Division 26 above. That is, reasonable requests for meetings should be accepted, with the regulations providing express criteria around determining reasonableness, including issues such as: those noted above in regard to the provision of information; the relative number and value of the requesting creditor's claims; and, security for costs being provided in cases where the request comes from a significant minority. As with Division 26, ASIC could be empowered to compel the holding of a meeting where it considers it reasonable. In every case, the meeting request must detail the agenda for the meeting and any proposed resolutions.
Division 30 – Committees of Inspection 30-10 – 30-35	This proposed amendment introduces additional complexity into the process of appointing a CoI which, in the absence of detail of regulations and consequential amendments to the current law, are difficult to assess. As it stands, it is unclear how it will work. Will creditors who may be on the Committee by statutory right be identified before or after the creditors resolve to have a committee and the number of people to be on that committee? Is it intended perhaps that those who have a statutory right join the committee are in addition to the number agreed by the creditors? Would those who have a statutory right initially put themselves up for election and, if unsuccessful on that basis, exercise their statutory right to join? The answers to these questions has implications for the appropriateness of the requirement to hold 50% of employee entitlements to participate on the CoI. On its face this requirement is very high for larger appointments because it would be impractical to obtain. We also note that a percentage of value criteria for membership also creates practical difficulties when there has been a

Section	McGrathNicol commentary
	limited response from creditors in submitting proofs of debt in response to the notice of meeting. It is inappropriate in our opinion to give supervisory responsibilities to the CoI. CoI members are not impartial and may be unrepresentative depending upon the level of interest in participating. Language such as 'giving a direction' should not be used as it creates an expectation that such direction will be complied with. The obligations of the EA's should be limited to taking into account the express wishes of the CoI. Giving creditors or CoIs the ability to replace or modify by resolution specific requirements imposed by regulations should be limited to procedural matters such as reporting frequency only. We are opposed to the proposal for the CoI to obtain specialist advice/assistance unless the EA is involved in providing the instructions, is given a copy of the advice and better arrangements are provided for meeting the costs of such advice. At present the cost is said to be an 'expense of the administration' but it is unclear what level of priority this will be afforded and what will happen if there are no available funds.

Chapter 3 – Regulator Powers and Miscellaneous Amendments

Section	McGrathNicol commentary
32-15 Court may inquire on application of creditors etc. 32-20A Meetings to ascertain wishes of creditors or contributories	The amendments need to be extended to address how the costs in relation to the application and inquiry are to be met.
32-22 & 32-23 Appointment of reviewing liquidator by ASIC, the Court or creditors	We submit that an EA under review should have the right to object to a proposed reviewing liquidator on the basis of conflict of interest, such objections to be subject to the reasonable review of ASIC. We recommend that 'expenses' be defined for the purposes of this provision. Expenses such as trading expenses in an administration may be subject to commercial confidentiality and the EA under review must have the ability to object (to ASIC) over disclosure (through a reviewing liquidator's report) of confidential information. The amendment should include provisions for a liquidator under review to be protected from reviews (as required by creditors resolution) which appear vexatious and/or which impose inordinate delay on the approval of fees. We submit that any regulations providing for an extension of the review period beyond the previous 6 months should be issued as a draft for comment prior to implementation.

Section	McGrathNicol commentary
32-24 Review	We submit that any definition of 'properly accrued' should be aligned with the IPA's guidance on remuneration for work that was necessary and properly performed.
32-27 Regulations about reviews	We submit that the proposed regulations be issued as an exposure draft for comment. The amendment does not include adequate detail as to the process and this should be subject to industry feedback as to practicalities before this new provision is implemented. We have noted (at 32-22 of our submission) that there should be a reasonable process for objecting (on the basis of conflict) to the appointment of proposed reviewing liquidators.
42-4 EAs to have regard to directions given by creditors or contributories	In our view language such as 'give directions to the EA' should not be used as it creates an expectation that such direction will be complied with. The obligations of the EA's should be limited to taking into account the express wishes of the creditors and contributories. Also we would favour the abolition of the use of the term 'contributory' and suggest it would bring Chapter 5 in line with other areas of the Act to refer only to 'members'.