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**When replying please quote**
**Our ref: NG:SAT:**
**Your ref:**

BY ELECTRONIC MAIL: phoenixing@treasury.gov.au

James Mason
Financial Systems Division
The Treasury
Langton Crescent
Parkes ACT 2600

Dear Sir,

We refer to your consultation paper – Combating Illegal Phoenixing – September 2017 which requests feedback and comments. Adopting your numbering system we comment as follows:-

**Phoenix Hotline**

1. Ineffective – 3.
2. No, however protection should be afforded to the whistleblower.
3. The benefit of a 'Phoenix Hotline' is that it allows the public the ability to bring suspected transgressions to the attention of the authorities. Currently such an option exists with the public having an opportunity to contact Australian Securities & Investments Commission (ASIC) with concerns. It does not appear however that ASIC the systems in place to properly deal with such complaints or otherwise does not act on such complaints. The risks are that illegal phoenixing activity is poorly defined and lay people may not be able to differentiate between an illegal phoenix and a formal / informal restructure, resulting in a significant number of calls to a hotline which could consume resources without cause or any result.
4. The major creditor left unpaid is more often than not the Australian Taxation Office (ATO), when a phoenix transaction occurs. Accordingly the ATO would be the best placed agency to properly resource and investigate phoenix activities. They would also have the ability to investigate the suspected phoenix entity's level of compliance with their tax obligations.
5. Reports on the number of calls, the outcomes of such calls including details of successful prosecutions should be published.

**A Phoenixing Offence**

6. Ineffective – 2
7. Whilst there is currently no definition of a phoenix transaction, in circumstances where assets are transferred at less than market value and creditors are left behind, liquidators appointed to the offending entity have the ability to report such breaches of director's duties (s180 – s184) to the ASIC. However, more often than not ASIC elect not to prosecute because of the dollar value involved or the lack of profile of the entity concerned. Further if the liquidator does not have sufficient funding, he is unable to commence legal proceedings in respect of the transfer of assets at less the market value. However with the new provisions allowing the liquidators to sell rights of action we may see increased activity in this space. Given the new laws are in their infancy it is too early to gauge the level of activity that may occur. The proposed new system is similar to the use of S139ZQ notices, however in practice, the use of such notices is not common. Further, the issue of a liquidator pursuing a claim in a fashion similar to s121 of the Bankruptcy Act is subject to the liquidator having sufficient funds to do so. In addition the usual operators of a phoenix scheme generally appoints a director of straw, thus a further offence carries little threat if any.

8. In the event that such a reform is introduced it is appropriate that Australian Securities & Investments Commission issues the notices, perhaps similar to the operation of notices issued in respect of obtaining compliance by directors to complete a report as to affairs or deliver books and records. This would occur where initial attempts for recovery by the liquidator are unsuccessful and they have referred the matter to ASIC for further action.
9. No – For consistency, one regulatory authority should oversee the process. That being said, where the phoenix transaction results in non payment of employee entitlements, an ability for FEG to recover the shortfall from the directors of the new and old entity as well as from the new entity should be introduced.
10. The liquidator should have the right to pursue any suspect illegal pheonix transaction, just as liquidators have the right to pursue any void transactions.
11. Commercial judgement should dictate the timeframe to respond and in the absence of an adequate response it is then a matter of commercial judgement for the liquidator to pursue the claim in court, similar to recovering a voidable transaction. Such a course of action though will be subject to the available funding the liquidator has.
12. If for commercial reasons the liquidator does not pursue the claim (e.g. insufficient funding in the administration) and ASIC issues notices that are not complied with, then a fine or penalty should be issued to the new and old entities as well as their directors. The quantum of the fine or penalty could equate to the value of unpaid creditors where it can be establish that the transaction occurred for less than market value.
13. Challenges that ASIC face include the public perception that they are a toothless tiger, who too often do not act on recommendations and offences detailed in liquidators section 533 reports or prosecute, allowing such transactions and pre insolvency advisers to flourish. ASIC may also have trouble commercially recovering money where the business or assets transferred are not readily capable of converting to liquid funds.
14. Yes – especially where the burden of proof to establish that the transaction was not a phoenix is transferred to the perpetrators.
15. If assets are transferred at market value and the proceeds paid to the company, then this transaction should be safeguarded. The issue is that often in these circumstances the ATO is still left behind as a significant creditor. If the ATO had better systems in place to monitor non compliance of taxation obligations and acted quicker through recovery actions which could ultimately result in winding up proceedings then the cost of phoenixing is reduced because the insolvent company has less time to accrue outstanding debt prior to it transferring assets and being wound up.
16. Yes – an additional offence should be introduced.

**Remedies**

17. Subject to appropriate safeguards, if the law is amended to enable directors to be personally liable for Goods and Services Tax (GST) in a similar manner to Pay As You Go Tax (PAYG) and Superannuation then this would be a sufficient penalty and often would also mitigate any advantage of orchestrating the phoenix transaction.
18. Yes
19. There may be significant evidence difficulties to establish "knowing involvement in a contravention" by advisers. If pre insolvency advisers are required to be licensed, a requirement that they produce their file could be introduced, failing which they could be deemed to be involved in the facilitation of the phoenix transaction. (similar to a presumption of insolvency where directors fail to produce books & records)

**Proposed Reform**

20. 5
21. Commentary around pre insolvency advisers suggest a significant instance of books and records being destroyed or simply withheld from liquidators, not withstanding that ASIC can issue notices to recover books & records. However in practice, where records are still not delivered, the recipient of the ASIC notice is issued with a nominal fine which is ineffective and hardly a

deterrent. To make this an offence could be an effective measure to enable ASIC to prosecute, however the effectiveness of the proposed changes will be subject to the applicable penalties.

Currently ASIC regulates by prosecuting "low hanging fruit" issue minor fines and then a press release highlighting statistics which indicates a high level of success. In reality they do not appear to have the RESOURCES, skill or desire to pursue more complex issues, as to lose such prosecutions will affect their statistics.

**Addressing Issue with Directorships**

22. 8
23. Yes
24. By changing the date of resignation to the date of lodgement or thereabouts (5 business days) this will stop the backdating and lodging of resignation documents, which currently allows for "dummy" directors being appointed well before the lodgement date, which has the effect of shielding the "actual director" from being personally liable for insolvent trading or personally liable in respect of Director Penalty Notices issued by the ATO.
25. 5 business days
26. The onus could be on both the individual director and the company.
27. Enforcement will occur when the ATO pursues the director in respect of a Director Penalty Notice (DPN) or where a liquidator issues proceedings against a director.

**Abandoning a Company**

28. 5
29. No.
30. Benefits include avoiding a situation where a company has no director. The risk is the director can not find someone to replace him and the company does not have sufficient funds to meet the costs of the winding up
31. By limiting a director's ability to resign without finding an alternate director forces them to comply with their obligations or wind the company up. Whilst it might be appropriate to make abandoning a company an offence, the penalty should not be an administrative fine, rather all the obligations and penalties associated with being a director should attach to the last registered director, or even extended to anyone who was a director in the preceding three months.
32. No
33. Unknown

**Restriction on voting rights**

34. 4
35. A registered liquidator is a highly qualified and regulated individual. The consequences of acting inappropriately are significant and can affect their ongoing ability to practice in the industry. In Bankruptcy and Part X administrations the monitoring of the legitimacy of related party claims is scrutinised by Australian Financial Security Authority when considering their entitlement to vote at creditors meetings. A similar approach would be just as effective with ASIC and companies. Currently the liquidator is required to scrutinise all creditors claims, including related parties and there are remedies for creditors to apply to court as a safeguard. Often in small businesses, related entities advance funds to assist with cashflow issues and have every right to vote, just like unrelated creditors. Often such funding is secured on the Personal Property Security Register (PPSR). To limit their voting rights may act as a deterrent to related entities from providing ongoing financial support, resulting in the company being wound up as opposed to riding out short term cashflow problems. Further, such an approach could result in unrelated creditors who perceive a bias, which in reality does not exist, exert too much power seeking to appoint a liquidator who they believe acts solely for them, resulting in a similar problem the proposed changes were attempting to fix.

36. Any change in the definition of related entity could result in manipulation to enable funds to have been advanced by "non related" parties as orchestrated by unscrupulous pre insolvency advisers.
37. All creditors whether related or not should all have the same rights for the reasons detailed above.
38. Levels of evidence to substantiate related party claims for voting purposes would be a matter of commercial judgement of the Chairperson of the meeting to determine, but would ordinarily include executed financial statements prepared by an external accountant detailing loan accounts and / or source banking records and similar documentation detailing evidence of the advance.
39. No – For the reasons detailed above.
40. Yes – In the majority of liquidations, creditors are not interested in participating / voting as they are aware of the company's financial position. In circumstances where there is unlikely to be a return to creditors, in the absence of related parties voting, it can be difficult for a meeting to have a quorum.
41. The Corporations Act should apply equally to all companies. To do otherwise will result in inequalities. There appears to be a significant misconception that size of a company has more or less issues or is more or less susceptible. This is generally not the case.
42. Yes – There should always be a safeguard and mechanism to appeal.
43. No – Same law to apply to all. Phoenix and related party creditors occur in both big and small companies. If the ATO ensured compliance in a timely manner, there would be no phoenix issues as there would be no debt to leave behind.
44. No
45. Orchestrated funding and a round robin of payments to "unrelated creditors"
46. Registered liquidators are required to complete, circulate to creditors and lodge with the ASIC a Declaration of Relevant Relationships & Indemnities (DERRI). Such a document should provide sufficient information to allow creditors and ASIC to determine the existence of collusion. Accordingly it should not be necessary to restrict related creditors voting rights.

**Promoter Penalties**

47. 6
48. Yes, definitely.
49. The benefit is that the reforms may act as a deterrent to promoters if they can be prosecuted for aiding and abetting illegal phoenix activities. The risk is associated with defining what is illegal phoenix activity. For instance if market value is paid for assets acquired by a related or similarly controlled entity and the funds are properly accounted for, but significant tax debt remaining unpaid – is this illegal phoenix activity? Similarly, what if the transaction avoided or minimised the crystallisation of liabilities such as employee entitlements or shorthfalls on finance agreements. The definition in Option One is very broad and would capture almost every company in liquidation i.e. most have unpaid tax obligations and unable to pay their obligations. The definition in Option 2 is an "intent test" which may be inherently difficult to prove.
50. Separate new provisions should be introduced.
51. Yes - Changes should include the introduction of licensing, minimum ongoing professional development requirements and insurance requirements to apply to pre insolvency advisers. In such circumstances there will be a level of accountability and consequences in the event that they transgress. The advisors who give poor advice are often unqualified "ambulance chasers" who prey on the desperate and vulnerable, and are not required to be registered or insured. In such instances they have no regard for the law or its consequences. Such changes should protect innocent advisers.
52. No.
53. Unknown
54. No. Often a company needs to be liquidated in a short period of time and an application to court may not fit this time frame. This process would also introduce a significant cost burden. Further, in many instances the phoenix transaction has occurred prior to the company being placed into liquidation.

**Extending the Director Penalty Notice regime to GST**

55. 8
56. The benefit of this proposed reform is that there is no benefit in phoenixing, if the intent is to leave ATO debt behind.
57. All directors, this promotes compliance which is a hall mark to good business and economic practices.
58. Yes, collect on a timely basis and expand the law to allow for the issuing of DPN's, garnishee notices and statutory demands to effect recovery. Similarly, similar to payroll tax, where a phoenix transaction occurs, group the related entity that acquired the assets to be liable for the outstanding obligations to the tax office.

**Security Deposits**

59. 7
60. The benefit of this approach is that it secures taxation liabilities. The risk is that it places an onerous burden on businesses, although it could be argued that such burden would not have been placed on them had they complied with their obligations.
61. Yes, it would assist and should be used as one of many tools for recovery.
62. One law should apply to all. If the company is in arrears, whether they meet the definition of High Risk Phoenix Operator (HRPO) should be irrelevant. A security deposit should be used just as other recovery tools are used against all companies.
63. Calculation issues in respect of future tax liabilities are a concern, and a high miscalculation could cripple cash flow and force a company out of business.
64. Refer to 63
65. Refer to 63
66. No, depending on circumstances assets could be sold to pay down debt and such measures could impact on secured creditors and / or employees.
67. Yes. Currently the ATO has powers in certain circumstances to require a security deposit, however they have been reticent to use this power. If used regularly, future expected tax refunds will be protected.

**Dealing with High Risk Entities**

68. 3.
69. "Straw Directors" will be used to avoid being captured as "High Risk entities". All companies should be subject to the same scrutiny.
70. Simply collect taxes on time and prosecute on a more timely basis the failure to lodge all ATO returns. If this occurs there is no incentive / benefit in entering into a phoenix activity.
71. Group the outstanding tax liability to the new entity in a similar fashion that the State Revenue Office does with payroll tax. In such circumstances the tax debt would survive the phoenix transaction. If this occurs there is no incentive / benefit in entering into a phoenix activity.
72. Yes – if such a designation becomes law
73. Defined

**Appointing Liquidators on a Cap Rank Basis**

74. 0 – To question the independence of all liquidators based on the actions of a small minority is offensive and wrong. Where a liquidator does not comply with his obligations, ASIC's role includes regulating such conduct. A "cab rank rule" would enable phoenix transactions to flourish. Unregulated pre insolvency advisers would facilitate a phoenix transaction, but the directors would then not appoint a liquidator. This would result in the transaction not being investigated in a timely manner. Further, liquidators would be unfunded. To suggest funding be provided via a component of the industry levy on corporations may be feasible but at what quantum would this be at? Registered liquidators currently perform a significant amount of

unfunded investigations and to continue to expect more unfunded work, when coupled with the requirement to fund the ASIC regulation of liquidators, makes for a large disincentive for liquidators to continue in this profession.

75 A more effective method would be for the ATO to monitor and enforce compliance in a timely manner. Further the ASIC should be more proactive in pursuing offences reported in s533 Reports lodged by liquidators.

76. This reads that "HRPO's" have already been decided on.

77. No – This would result in a delay on appointments and more unfunded work. In addition to the ASIC being reluctant to prosecute, the ATO is reluctant to fund liquidators' investigations and recovery work. It is unfair that liquidators get labelled for a "perceived" lack of independence, when often they have sought indemnity funding from creditors which has not been forthcoming and reports lodged with ASIC recommending prosecutions are not acted on. In such circumstances the major stake-holders in the liquidation don't show an active interest in the matter, however significant law change is suggested, inferring a lack of independence by the liquidator, however it is the inactivity of the creditors and the regulator which prevent an unfunded liquidator from acting further. Furthermore, recent changes to the Corporations Act 2001 provides creditors with greater capacity to replace incumbent liquidators and receive more timely reports and access to information.

78. No. Directors should be able to seek advice and select a qualified professional who is sufficiently regulated to undertake a liquidation.

79. Should not be in existence and the question reads as if it is already in place.

80. Funding should not be provided by the registered liquidator. The ASIC continues to indicate that pre insolvency advisers have perpetuated phoenix activities. Such people should be governed by a form of regulation and be required to be registered / licensed. Further, just as registered liquidators are required to fund investigations into overseeing and regulating registered liquidators, registered pre insolvency advisers should be required to fund the associated costs of funding a system to eradicate phoenix transactions created by them.

**A Government Liquidator**

81. 0

82 Whilst the official receiver performs a similar role in Bankruptcy, complexed estates are often transferred out to registered trustees to administer. The previous senate review widely criticised the ASIC role in relation to external administrations and the question is whether the ASIC have the ability, funding and resources to perform this role effectively.

83. No. Refer to above.

84. It may be that in the event that a government liquidator is created, it consents to acts as liquidator of Court appointments. This may be on the basis that registered liquidators refuse the consent to act in circumstances where they are not funded, yet still are expected to perform a statutory minimum level of investigations. Additionally registered liquidators are required to pay from their own pocket lodgement fees on notifiable events.

85. Funding should be sourced from asset realisations or requests be made to creditors, just as in all other liquidations. Should ASIC seek to recover costs that are not met from asset realisations then a levy on companies which could be attached to companies annual return is one option. The other option is that all company directors are required to complete a basic course on their obligations and the consequences should they breach the law before obtaining a director ID number. The fee to perform this course could meet ASIC costs and further hopefully with this education and awareness directors may act a bit more responsibly which may decrease the prevalence of corporate failure.

**Removing the 21 Day Waiting Period for a DPN**

86. 6.

87. This question again indicates that treasury appears to have made up its mind that there will be a classification HRPO.

88. The risk of this approach is that "people of straw" will be appointed to companies by those whose intent it is to abuse the system. Having said that such people would breach the law regardless of the consequences.
89. No.
90. It is not that simple to transfer assets of value in a 21 day period. For example to transfer a house with a mortgage registered on title would require the consent of the mortgagee or refinancing. Both options in reality do not happen within 21 days. Even where assets are transferred during that 21 day period, such transfers would be voidable against a bankruptcy trustee. If the ATO monitored compliance in a timely manner then such efforts to recover unpaid taxes would not be required.

**Providing the Australian taxation Office with the power to retain refunds**

91. 9.
92. Yes, but the system should be extended to all directors, but it has the ability to affect the company's cashflow.
93. Benefits included increased compliance and collection of revenue. It also acts as a disincentive to create a phoenix transaction because statutory payments would not be significantly in arrears.
94. Yes–Subject to safeguards and a right of appeal.

**Our suggestions to effectively limit phoenix activity**

- Introduce Director Identification Numbers
- Require directors to complete a brief course which educates them of their obligations and consequences if they transgress. The costs of this course would assist in funding investigations.
- License pre insolvency advisers, similar to financial planners.
- Make it an offence for anyone other than lawyers, a licensed pre insolvency advisers or registered liquidators to provide insolvency advice.
- Group outstanding taxation obligations so that the new entity is liable for the debt left behind in the phoenix transaction.

Yours faithfully

Dye & Co Pty Ltd

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