

27 October 2017

The Treasury
Financial System Division
Langton Crescent
PARKES ACT 2600

by email: phoenixing@treasury.gov.au

Att: James Mason

Dear Sir

Combatting Illegal Phoenixing

We respectfully make this confidential submission in response to the consultation paper issued on 12 September 2017.

Ferrier Hodgson supports the Australian Government's action to crackdown on illegal phoenixing activity. Ferrier Hodgson concurs that a whole-of-Government response is required to combat this activity.

We are generally supportive of the proposal for reform. Unless we have commented specifically in this submission, we concur with the position taken by the Australian Restructuring Insolvency & Turnaround Association (**ARITA**) in their submission on the consultation paper.

It is Ferrier Hodgson's view that a significant part of the problem with illegal phoenixing activity is caused by:

1. The ATO who is generally the largest creditor in a phoenixed company not having the systems to identify at a much earlier stage that a company who is registered for GST or PAYG is not lodging returns or making payments. There does not appear to be any cross checking between Government agencies to identify whether a company is trading or one that is not. We have seen in many instances companies we have been appointed to as Liquidators not having paid their taxes for years and the ATO being used as their 'other bank', notwithstanding these companies have large numbers of staff, commercial bank facilities, lease and loans.
2. Liquidators continue to be frustrated by ASIC's responses to Section 533 reports where offences have been identified after detailed investigations have been carried out, only to have ASIC chose 'not to take any further action'. This frustration is exacerbated when in some cases Liquidators identify that there has not been any offence nor further investigations required, yet ASIC unnecessarily requires a 'supplementary report' to be prepared adding additional unrecovered costs.
3. The Assetless Administration Fund is difficult to access and any funding available is insufficient to enable proper investigations and prosecutions to occur. This results in directors knowing that a Liquidator has no funds to pursue any illegal activities. Serious considerations should be given to reforming the process and granting greater funding.

Whilst the consultation paper acknowledges that the overwhelming majority of Liquidators do the right thing, there does not appear to be any acknowledgement that those very same liquidators do not recover a significant portion of their fees when administering most liquidations.

With reference to the Phoenix Taskforce which has been established since 2014, Ferrier Hodgson is concerned that:

- The agencies are not working in an entirely co-operative manner – agencies are still seeking to protect their patch rather than sharing resources and supporting actions identified by other agencies;
- Because of the failure of the agencies to co-operate fully, activities undertaken by the taskforce are significantly delayed in their response which opens the agencies involved to criticism for an apparent lack of agility to address illegal phoenix activity in a timely manner;
- There is insufficient funding available to enable the agencies within the taskforce to adequately resource the work that needs to be undertaken to make a difference and have an impact on illegal phoenix activity.

About Ferrier Hodgson

Ferrier Hodgson is one of Asia Pacific's leading providers of restructuring and business advisory services. Since 1976 we have developed a reputation for solving complex financial and operational problems with commercial solutions that deliver value and results to all levels of stakeholders.

Our key service lines are:

- Restructuring, turnaround and insolvency
- Forensic accounting
- Forensic IT
- Management consulting
- Corporate and transaction advisory

In response to the consultation paper, we advise as follows:

1 Broad reforms

1.1 A phoenix hotline

Question 1 – On a scale of one to ten, where one is 'ineffective' and ten is 'highly effective', please rate how well you think this measure will operate to deter and disrupt illegal phoenix activity?

Ferrier Hodgson rates this new measure as one – ineffective. A hotline already exists for interested parties to contact ASIC on an anonymous basis. The most critical issue of any hotline is to ensure the information gathered is shared collaboratively by the relevant government agencies and those agencies are seen to work collaboratively in sharing and acting on the information.

Question 4 - Which agency do you believe would be best placed to operate such a hotline?

Ferrier Hodgson considers that if a 'phoenix hotline' is to be established the ATO is the agency in a better position to operate it. The ATO is most impacted by illegal phoenix activity and the consequent loss of revenue to the Commonwealth has far reaching consequences for the economy as a whole.

The ATO is best placed to undertake initial enquiries into intelligence received through the hotline. The ATO can access the taxpayer records and identify the status of lodgements and payments and match that information to taxpayer banking data to ascertain the level of activity through taxpayer accounts and whether that appears consistent with the lodgements and payments recorded by the ATO.

From there the ATO can share more detailed information with the other agencies as relevant for investigation and action.

1.2 A phoenixing offence

Question 6 - On a scale of one to ten, where one is 'ineffective' and ten is 'highly effective', please rate how well you think this measure will operate to deter and disrupt illegal phoenix activity?

Ferrier Hodgson rates this measure highly.

Question 8 - Should ASIC retain control of the issuing of such notices to ensure that they are not issued inappropriately?

Ferrier Hodgson considers that ASIC should control the issuing of administrative recovery notices. It is our opinion that a company (and its directors) that may have been involved in illegal phoenix activity will be more likely to respond to a notice issued by ASIC than a notice issued by the registered liquidator who, those parties will assume, is in all likelihood unfunded and therefore unlikely to take any steps to respond to the notice.

Question 10 - Should liquidators have the ability to independently issue such notices in cases where they suspect that illegal phoenixing has taken place?

See our submission for Question 8 above.

Question 13 – What are some of the challenges ASIC is likely to face in seeking compliance with the notice?

ASIC's major challenge are its internal resources i.e. funding and staffing to pursue matters.

1.3 Addressing issues with directorships

Question 31 – Should abandoning a company instead be an offence?

Ferrier Hodgson believes that if sole directors are unable to resign unless they find an alternate director or appoint a liquidator but still chose to abandon their company then this should constitute an offence.

1.4 Restrictions on voting rights

Ferrier Hodgson concurs with ARITA's responses on this matter.

1.5 Promoter penalties

Ferrier Hodgson generally concurs with ARITA's response on the proposed reform of the promoter penalty laws. However, ARITA's reliance on the fact that the existing laws are adequate and its citation of ASIC's successful prosecution of a solicitor who advised directors on phoenix activity (ASIC v Somerville [2009] NSWSC 934) seems inconsistent with our recent experience.

In a court liquidation currently being administered by Ferrier Hodgson we have undertaken examinations of two directors and their advisor. During those examinations, there were clear admissions that the directors acted on advice from their advisor to enter into transactions to transfer the business and assets

of the liquidated company to other entities for no consideration to avoid the payment of debts due to the Workers Compensation Nominal Insurer (**WCNI**).

ASIC had expressed interest in the case and the liquidator had provided ASIC with a supplementary report pursuant to Section 533(2) of the Corporations Act 2001. After the examinations, the liquidator also provided ASIC with a copy of the transcripts of the examinations of the directors.

Notwithstanding the admissions made by the directors, ASIC elected not to proceed with any prosecution because:

- The directors were in ASIC's view only acting on the advice of the advisor. But for that advice they may never have elected to enter into the transactions. The area of ASIC looking at this matter only dealt with criminal convictions and they did not consider there was enough evidence to obtain criminal prosecutions against the directors;
- The advisor was not a director of the company so the ASIC personnel did not consider that they could take any action against him. This was notwithstanding that the liquidator had raised the Somerville case with the ASIC officers.

Unless the regulator is prepared to enforce and prosecute under the existing laws there will be no impact on illegal phoenix activity. In the case referred to, the liquidator is continuing civil prosecution against the directors and the advisor with the support of the WCNI.

1.6 Extending the DPN regime to GST

Ferrier Hodgson concurs with ARITA's responses on this matter.

1.7 Security deposits

Ferrier Hodgson concurs with ARITA's responses on this matter.

2 Dealing with higher risk entities

2.1 Targeting higher risk entities

Ferrier Hodgson concurs with ARITA's responses on this matter. However, whilst the existing laws should guard against the abuse of the corporate form, the general lack of action by ASIC in addressing matters raised in Section 533 reports implies that many potential repeat offenders will continue to operate outside the prevailing laws.

2.2 Appointing liquidators on a cab rank basis / a Government liquidator

Ferrier Hodgson concurs with ARITA's responses on this matter.

2.3 Removing the 21-day waiting period for a DPN

Ferrier Hodgson concurs with ARITA's responses on this matter.

2.4 Providing the ATO with the power to retain funds

Ferrier Hodgson concurs with ARITA's responses on this matter.

Thank you for the opportunity to present our submissions on the consultation paper for Combatting Illegal Phoenixing.

Please do not hesitate to contact me if you have any questions or would like me to expand on any of the points contained in this submission.

Yours faithfully
Ferrier Hodgson



R Duggan
Partner