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12th October 2020

Our Ref: Ray Barrett
The Manager
Treasury
Insolvency Law Reform
By email only: MCDInsolvency@Treasury.gov.au

Dear Sir,

CORPORATIONS AMENDMENT (CORPORATE INSOLVENCY REFORMS) BILL 2020
EXPOSURE DRAFT EXPLANATORY MATERIALS

I write in relation to the abovementioned Bill and explanatory materials.

By way of background I am a registered liquidator (IP) and legal practitioner, and I have worked but not exclusively, in the insolvency area since the early 1980s.

Having regard to the short time frame for comments on the Bill, I do so in an abbreviated format.

1. **Schedule 1- Restructuring Company**

1.1 **Insolvent Corporate Trustees**

The evidence is that a substantial number of companies in the cohort to which these amendments are directed will be corporate trustees of discretionary and unit trusts. As Treasury will be aware, typically trust deeds have a provision to the effect that on the trustee suffering an insolvency event including a compromise of its creditors, its position as trustee is automatically vacated.

This has led to a substantial body of law and uncertainty and notwithstanding the decision in *Re Amerind,* insolvency practitioners still face the prospect of applications to Court for authority to deal with trust assets. The restructuring as envisaged by these measures will confront that same uncertainty and controversy.

To me the options available are:

1.1.1 **Do nothing**

I suggest that a "do nothing" approach will continue the present uncertainties for directors and IPs dealing with insolvent corporate trustees. I am concerned that with SBRPs not having sufficient experience to identify the complex issues arising from insolvent corporate trustees that a "do nothing" approach will have unintended adverse consequences.

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I accept that it is open to parliament to say that the directors of such corporate structures, having made a decision to adopt them, are precluded from the new restructuring option and will have adopt the existing VA or liquidation process and if Court approval is required for any particular step then so be it. However, I suspect with this approach a significant proportion of the cohort that these provisions are intended to assist will miss out.

1.1.2 **Addressing the Issue**

The Bill could accommodate insolvent corporate trustees (I accept that there may be constitutional uncertainties/challenges) by:

i) In the proposed s452B - in the definition of property include as property a company's right of indemnity (both as to recoupment and exoneration),

ii) Those sections dealing with notices to creditors and members should include notices to specified beneficiaries,

iii) In s454S (3) include the words "instrument or deed" after the word "a" in the first line.

1.2 **Other Comments**

It is possible that the marketplace will develop processes to deal with this issue. For instance:

Prior to the appointment of the SBRP, the company could amend the trust deed so that the entering into a restructuring plan does not trigger the automatic vacation of the office of trustee.

The difficulty with this is that those advising the corporate trustee and its directors, will be reluctant to give that advice particularly in circumstances of insolvency or near insolvency. It may be seen, perhaps incorrectly, as a last-minute transaction that warrants interference alternatively, in circumstances where the corporate trustee may be insolvent in its own right and trustee of a trust that is solvent then there are genuine reasons for the insolvent corporate trustee to be removed from the office as trustee. So, I think a marketplace solution is unlikely – or at least a well-advised marketplace.

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I reiterate as a general observation that if corporate trustees or the SBRP see the necessity to apply to the courts to seek directions, authority to do things and/or appointment as receiver of the trust then the measures will be uneconomic for this cohort and not adopted.

2. **Schedule 3 – Simplified Liquidation**

2.1 **Insolvent Corporate Trustees**

The same difficulties identified above in relation to corporate trustees will apply to these measures.

2.2 **s500AA Eligibility Criteria for Simplified Liquidation Process**

Subsection 500A(1)(f) will be a difficult hurdle for many small companies.

The costs of preparation and lodging outstanding taxation documents can be a substantial hurdle particularly if a number of years income tax returns are outstanding.

In circumstances where companies have been trading at a loss for some period of time, perhaps years, and there is no income tax payable, it is often the case that income tax returns are outstanding as being something that is seen by the directors as an unnecessary expense. I think that this provision is likely to increase the number of abandoned companies.

Perhaps there is a compromise that the subsection should be limited to outstanding Business Activity Statements rather than 100% compliance with all taxation laws.

In the unlikely event that the liquidator observes that the company may be liable for income tax and the estimated liability then pushes the company's total liabilities above the threshold then there will be a transition to a standard CVL.

3. **Regulations**

Much of the eligibility and details of the restructuring plan are to be the subject of the regulations (draft not yet published) and I make the following comments in relation to the proposed regulations in the light of what has is outlined in the Bill and what has been said in the Federal Government's announcements:

3.1 Consideration should be given to increasing the cap on liabilities to $A2 million. I say this because a company in the $A1 million to $A2 million zone (and which does not qualify) will have to confront the high costs of VAs and the existing barriers to restructuring will continue for this cohort. In my observation a business with liabilities of $A2 mil is unlikely to have the asset base that can support the present VA process.

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3.2 Employee entitlements that must be paid should be defined as those entitlements that are due and payable. In particular accrued LSL, holiday pay and redundancies ought not be regarded as unpaid unless the liability has crystalized and not paid. In my experience most wages and leave entitlements are paid for those employees actually taking leave. In any event amounts not paid for these categories can usually be brought into compliance.

3.3 In the case of redundancy entitlements, not yet crystalised, if these are to be included as either paid employee entitlements or as part of the liability cap then it may well skew the cohort of companies that are able to access the new measures and in an arbitrary way.

For example, a company with liabilities approaching $A1 million (which may be seen as a higher risk profile) but with less than 15 employees, say 5 employees, which is not obliged to pay redundancy entitlements (unless the employment contract says otherwise) would be eligible but this is in contra distinction to a company with say $500,000 of liabilities (which may be seen as a lower risk profile) and 20 employees, and subject to redundancy obligations that cannot be paid, would not be eligible for the scheme.

This appears to us to be an adverse arbitrary result - the firm with the most employees and the lower risk profile cannot take the advantage of the regime whereas the firm with a higher risk profile and least number of employees will be able to do so.

3.4 Consideration be given to assessing liabilities on a **going concern basis** so that ongoing premises rent, leasing/finance costs for plant, equipment and motor vehicles and any finance debt that stretches beyond the end of the restructuring plan would not be included in the liability count nor any entitlement to vote nor participate in a distribution. This will bring more entities into the scheme and without any undue measure of risk as the premises rent, finance costs and loan repayments will have to be paid during the implementation of the plan in any event. Those creditors will have to be satisfied on an ongoing basis as for the most part they will have remedies not defeated by the new measures.

3.5 **Superannuation Guarantee Contributions (SGC)**

If the SGC is included in the list of employee entitlements that need to be paid then, a number of small businesses will not be able to meet this hurdle. The solution here is to extend the recent but now closed SGC amnesty and for the regulations to provide that it will not be a barrier to entering into the restructuring regime if the company has SGC liabilities but has entered into an amnesty payment plan.

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4. **Functions, Duties and Powers of the Restructuring Practitioner**

I believe it to be unsatisfactory to identify the powers of the SBRP in the regulations in circumstances where s453E(1)(a)-(d) provides little guidance.

I think the better approach is to look at s477 of the Act and identify those powers that should be explicitly identified in the Bill particularly in circumstances where the company being restructured is limited to only doing those things that are in the ordinary course of business.

It occurs to me that at the very least a SBRP ought, subject to the proviso that such steps are in the interests of the company as a whole, be able to do the following:

4.1 authorise the directors to institute legal proceedings in the name of the company and at the cost of the company;

4.2 at the cost of the company appoint a solicitor or expert to assist him or her in his or her duties. An expert with a particular technical background might be needed in order to certify the viability of the restructuring plan.

In closing can I say that I think that the thrust of the legislation to a "debtor in possession" model has much merit and I hope that it can be made to work.

Yours faithfully,

Ray Barrett.

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Lawyers