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12 October 2020

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Via email: matthew.bowd@treasury.gov.au

Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 Exposure Draft and Explanatory Materials

Dear Matthew,

CPA Australia represents the diverse interests of more than 166,000 members working in over a 100 countries and regions around the world. We make this submission on behalf of our members and in the broader public interest.

CPA Australia agrees with the nature and direction of insolvency law reform represented in Schedule 1 (Restructuring of a company) of the Exposure Draft. We are also broadly supportive of the recognition given in Division 4 Subdivision A as to who may be appointed a restructuring practitioner (currently proposed as being narrowly based, per section 456B) along with the interrelated measures identified in Schedule 3 Item 8 concerning repeal of subsection 20-20(5) of Schedule 2 of the Corporations Act 2001. The intention, as we understand from the discussion in Chapter 4 of the Explanatory Materials, is to achieve what may cautiously be termed a second-tier of insolvency practitioner.

We feel it is important to elaborate further on those matters pertaining to the role of a small business restructuring practitioner (hereafter **SBRP**), briefly discussed in the Factsheet accompanying the Treasurer's 23 September announcement of the reforms, and the apparent ensuing debate around the source and breadth of practitioner/adviser who may perform these roles.

Whilst supportive of these measures, we note that they only apply, and correctly so, at the point where an entity is insolvent. Equally important in assisting Australia's economic recovery and building a vibrant small business sector, are practices of early intervention ahead of actual insolvency and measures designed to enable fair and realistic assessments of business viability. To this end, we also consider it important that there be an appropriate source of professional services and for existing measures being reviewed and potentially enhanced to combat wrongdoing in the sphere of pre-insolvency advice.

1. **Structure and instruments through which the reforms are to be achieved and the supporting regulatory mechanisms by which the proposed Part 5.3B restructuring of a company are to be applied**.

We refer specifically to those matters discussed in paragraphs 1.104 through 1.112 of the Explanatory Materials under the heading *Miscellaneous.* We are concerned that what is described in these paragraphs lacks suitable certainty in substantive laws affecting the rights and remedies of affected parties, and indeed, that the foreshadowed processes of legal rule development risk lacking transparency, potentially undermining confidence in the law.

CPA Australia acknowledges that dealing with the economic consequences of COVID-19, and the need to position the business sector for recovery in 2021, necessitates both compressed law reform timeframes and flexibility to developed rules, processes and procedures progressively. Nevertheless, in CPA Australia's view, where possible those matters identified across paragraphs 1.104, 1.106, 1.107, 1.108 and 1.109 of the Explanatory Materials, ought ultimately to be expressed in the statutory provisions of the Corporations Act rather than prescribed by regulation. What is very concerning is the remark in para. 1.110 establishing that, in instances of inconsistency, the regulations will prevail over that which is in the Corporations Act, and that a sufficient safeguard exists for disallowance through parliamentary scrutiny (refer para. 1.112). As matters of both development of sound law and public confidence, such proposed shifts between Parliamentary and executive powers should be widely canvassed and debated. In the likelihood that there will not occur, in the short term, significant shifts in the structure and application of this corporate insolvency law reform, CPA Australia suggests, as a worthwhile safeguard, the embedding in proposed Part 5.3B of independent review mechanisms along similar lines to that provided for in section 588HA in relation to the insolvent trading safe harbour introduced in 2017.

CPA Australia offers a limited number of observations and suggestions that we believe could improve the operation and chances of successful small business restructuring within the proposed Part 5.3B. This includes reference to what we regard, at least at this early stage of development, will be some of the more salient features of a restructuring plan, and the rules and guidance which are presently intended to be articulated primarily through regulations.

- The matters to be resolved by regulation are extensive and mirror, as emphasised in the Explanatory Materials, many features of the Part 5.3A. Other than achieving the 'debtor-in-possession' objective expressed in section 452A(a), primarily through operation of proposed sections 453K and 453L(2), it is unclear whether a suitable level of simplification has been achieved. In comparison, this advancement in process seems, on an initial review, to be more apparent with the simplified liquidation laid out in Schedule 3.
- Proposed section 453A addresses when the restructuring of a company begins and ends with Division 3 of Part 5.3B, which deals with the restructuring plan itself, in turn identifying a wide range of matters to be dealt with by way of regulation, including termination. We suggest, in developing these rules and guidance, a greater degree of specificity around timeframes, to lessen some of the risks of open-endedness which may prove unduly disadvantageous or burdensome on a debtor company.
- Proposed section 453C foreshadows the prescribing by regulation of the level of liability criteria for a company to be eligible for restructure. We suggest that either in this section, or appropriately elsewhere, cross-referencing to section 455A(2) in Division 3 (Restructuring plan) reiterating the point of eligibility being dependent on proven insolvency, and that moreover, a company would be ineligible if it has not maintained adequate financial records.
- Proposed section 453H establishes the SBRP's capacity to act as a company's agent, whilst section 453K proposes for the company to retain control of its business, property and affairs. Aside from establishing the necessary capacity for the SBRP to bind the company in contract, we

query whether either in the legislation or in regulations, the threshold of powers between directors and the SBRP could be better addressed.

- Subsection 3 of proposed section 455B (Restructuring plan) envisages the making of regulations in relation to the treatment of debts and claims within a restructuring plan. In doing this, we urge caution in allowing departure from the well-established structures and methodologies for proving and ranking of claims set out in detail in Division 6 of Part 5.6 (Winding up generally).
- Subsection 4 of proposed section 455B anticipates regulatory provisions regarding the treatment of contributories. We again urge caution, in this instance in the development of rules and guidance concerning the ongoing obligations and liabilities associated with a restructuring plan. It can reasonably be anticipated that there is a greater likelihood for small businesses, when compared to those companies which may avail of a deed of company arrangement (DOCA), being more cash flow dependent over short time horizons and with fewer assets to operate as buffer if the restructuring suffers operating stress, thus posing issues of vulnerability which ought be protected at a reasonable level.
- Subsection 7 of proposed section 455B foreshadows the promulgation of regulations dealing with a range of matters associated with the SBRP's involvement with a restructuring plan. Either within this regulation, or within the following Division 4 of Part 5.3B, we strongly suggest there should be addressed the various matters which both recognise and support the notion of a 'fit and proper' person capable of engagement in these appointments. Aside from consistency with matters potentially dealt with in Schedule 2 (Insolvency Practice – Corporation) to the Corporation Act 2001, and the accompanying ASIC Regulatory Guide 258, there needs to be sufficient articulation of expected standards of conduct. These should identify such matters as adherence to a code of professional conduct, the carrying of professional indemnity assurance, and complementary industry association licensing, including application of practice quality review and disciplinary procedures, and in this latter matter, capacity for notification to ASIC along the lines of Schedule 2 Clause 40-1/ Rule 40-1.

2. Small business restructuring practitioner

In expressing an underlying policy intention of simplification, the Factsheet sets out interrelated boundaries of operation, whereby a presumption is made that corporate insolvencies below a particular dollar threshold may involve less complexity, and thus can be streamlined, and that it is accordingly appropriate for a class of practitioner to be recognised as qualified to undertake this type of engagement, though not able to perform more complex work that is the traditional domain of a registered liquidator.

CPA Australia suggests that understanding the boundaries of this endeavour to have more practitioners available to work with small businesses is best derived from reference to the words and structure of Part 5.3B itself. The tendency in the development of Australian corporate insolvency law to safeguard the interests of unsecured creditors is, in our view, justifiably carried over into these latest reforms. The object set out in section 452A clearly enunciates the purpose of enabling the insolvent company to enter into a restructuring plan with creditors. More particularly, from the standpoint of the SBRP's interaction with the rights and interests of creditors, are proposed provisions such as section 453J dealing with the practitioners' power to terminate the restructuring when deemed not to be in the interest of creditors, and section 453N(9) requiring the practitioner to consent to alterations to the status of members under a restructure only where reasonably believed to be in the interests of the company's creditors as a whole.

The above points to requirements for both familiarity with the broader operation of corporate external administration, along with the wider scheme of Australian corporate law, and high levels of professional judgment. Therefore, in advancing those matters canvassed in Chapter 4 of the Explanatory Materials around greater flexibility in the Schedule 2 committee assessment criteria and decision making, CPA Australia believes that an important avenue for facilitating greater availability of practitioners, whilst at the same time safeguarding the integrity of the new small business restructuring scheme, will be to

encourage, if not indeed favour, applicants holding an industry body public practitioner license and who also have a substantial established professional relationship with a registered liquidator, with him or herself being able to provide suitable supervision and mentoring.

It will be evident from the foregoing discussion, that CPA Australia sees the role of the SBRP as distinct, and at arm's-length, from professional advisory services providing pre-insolvency advice generally, or who under the current economic conditions may be providing viability assessments ahead of a small business considering restructuring within the ambit of the proposed Part 5.3B. These latter activities serve an important role in both early intervention and in the making of realistic assessments of a capacity to trade-out of financial difficulty. The conduct of participants should likewise adhere to the highest standards of ethical conduct and CPA Australia remains concerned as to the extent to which the current economic circumstances leave companies and their directors prone to receiving either incompetent, or indeed reckless, advice. As such, we urge that appropriate attention be given to effective enforcement of the procuring provision under the anti-phoenixing provisions enacted earlier this year, along with a realistic assessment of how best to deal with the inevitability of what will be a very large number of abandoned companies.

CPA Australia is grateful for the opportunity to make this submission. If you require further information on the views expressed, please contact Dr John Purcell FCPA, Policy Adviser ESG at john.purcell@cpaaustralia.com.au.

Your sincerely

Dr. Gary Pflugrath
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