Small Business Insolvency Reforms 2020

Response and Key Recommendations for Improvement

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Background & Key Recommendations

Background

SV Partners welcomes the opportunity to respond to the Federal Government's proposed changes to the small business restructuring process and simplified liquidation reforms as detailed in the Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (**the Reforms**).

We note that Treasury has not yet released for consultation the Regulations or Rules for the Reforms and that these documents will likely contain the bulk of the details. It is imperative that Treasury provides this information to the Profession as soon as possible so that we may provide feedback.

We generally support the Explanatory Memorandum's stated reforms of incentivising business owners to deal with their financial affairs (rather than burying their head in the sand until it is too late) and reducing the barriers of high cost that presently come with simple liquidations. Despite these stated intentions, it is our view that the Reforms are unlikely to meet the purpose hoped by Government.

Instead, a 'root and branch' review of the insolvency laws are needed, as set out in the Australian Restructuring, Insolvency and Turnaround Association (**ARITA**) 8 point plan, 'Financial Recovery 2020'.

Further information about SV Partners is set out in the final pages of this submission paper.

Key Recommendations

The following pages contain a full list of issues that we have identified in the Reforms, and the following lists our key recommendations:

1. The proposed new Restructuring regime requires a business owner to pay their business' employee entitlements before they are eligible

   Issue #10 within the below recommendation table deals at length with this issue, particularly around the meaning of 'employee entitlements'. If this eligibility requirement is maintained in the final legislative instrument, it is doubtful that many small business owners will qualify. In our experience, very few financially distressed companies have paid, for instance, all of their superannuation or wage entitlements upon an external administration appointment.

   Recommendation: adopt a 5% of total liability test to the eligibility requirement for employee entitlements and narrow same to just unpaid wages and superannuation

2. The proposed new simple liquidation (SL) regime requires a director(s) to have lodged all of their taxation returns before they are eligible

   Issue #25 within the below recommendation table deals at length with this issue. If this eligibility requirement is maintained in the final legislative instrument, it is doubtful that many small business owners will qualify. In our experience, very few financially distressed companies have lodged all of their business activity statements and taxation returns before the appointment of an External Administrator.

   There is also limited incentive here for a business owner to rectify their lodgement history if they are winding up their company, because (at least): (a) the cost of conducting the Liquidation rarely impacts on the director, as opposed to creditors; (b) the cost of lodgement by an external accountant typically exceeds $5k for each year outstanding; and (c) lodgement could open those directors up to director penalty notices by the Australian Taxation Office (**ATO**).

   Recommendation: remove this requirement entirely, as it is contrary to the stated purpose of simplifying small liquidations.

Key Recommendations

3. The proposed new SL regime excludes Court Liquidations (CL)

   Issue #26 argues that an SL must be expanded to include CL's. We do not understand the policy decision around why a Liquidator in a CL cannot simply write to creditors in the first report to creditors proposing to use the SL, as long as they reasonably believe it is in the best interest of creditors. Safe guards can be included in the event total liabilities or other eligibility requirements are not met at a subsequent date.

   Recommendation: expand SL's to include CL's

4. 453LA(1)(a) erroneously refers to 453 not 453L

   Issue #19 explains the issues identified in this provision. We strongly urge Treasury to include a new s553C(3) provision that specifically excludes ss 468, 453L and all of Part 5.7B of the Corporations Act, otherwise creditors and related party stakeholders will continue to exploit these provisions following the erroneous decision of Morton v Rexel Electrical [2015] QDC 49.

5. The new small business restructuring practitioner (**SBRP**) must be an appropriately qualified, experienced and licenced Registered Liquidator (**RL**)

   Issue #5 argues that a SBRP must be an RL, and we adopt the submissions of ARITA in this regard. It is very important that the Government does not water down these provisions to allow dodgy, unlicenced, pre insolvency advisors and illegal phoenixing enablers to qualify.

   Given the proposal to creditors for the Plan is likely to contain 'forward looking statements' (ie comparison of alternative options for creditors, cash flow budgeting, significant engagement with key stakeholders, exercise of a professional judgement), we do not see how a non typical RL will be able to produce and swear to these proposals.

   Issue #4 queries whether a SBRP will be required to pay the ASIC insolvency practitioner levy?

   Recommendation: adopt the submissions of ARITA in relation to the registration requirements of the SBRP, along with the suspension of the ASIC insolvency practitioner levy

6. We urge the government to suspend the ASIC levy for at least 1 year (or indefinitely)

   Issue #4 argues that the ASIC insolvency practitioner levy must be suspended for at least 1 year to enable the Profession to recover after a number of lean years (particularly given the moratorium on insolvency). We estimate that the majority of active RL's are paying in excess of $25,000 per year each towards this levy. As ASIC provides no transparency to its remuneration, RL's find it difficult to plan, and budget, for this levy each year.

   Given Treasury and the Government have openly stated that they are concerned by the lack of RL population, this proposal will go a long way to fixing this issue.

   Recommendation: suspend the ASIC insolvency practitioner levy indefinitely until the RL population issue is addressed

Key Recommendations

7. We urge Treasury to release its modelling on what cost savings are expected from 500AE(2)

   Issue #27 deals at length with this issue. We are underwhelmed by the proposed SL exclusions to a typical CVL. Very rarely are creditors meetings or Committees of Inspection (COI) utilised in a CVL, and the exclusion from having to prepare a 533 report and EX01 for ASIC will provide minimal costs savings. A conservative RL is likely still going to be producing their own 533 report to ensure they have not missed anything that should otherwise be reported to ASIC or could be recoverable for the benefit of creditors.

   Instead, a bigger cost saving would be to combine the initial and statutory reports (similar to the bankruptcy laws) and reduce those reports to a capped number of pages (of say 5 pages, excluding simple fact sheets, to be prepared and provided to the Profession by ASIC).

   Increasing the minimum remuneration automatic approval from the current approximately $5.3k (exc GST) to $10k (exc GST), would drastically reduce the size and complexity of SL's.

   Recommendation: Treasury to urgently release its cost saving modelling and seek stakeholder feedback on increasing the automatic minimum remuneration approval

All Recommendations

In additions to the above 7 key recommendations, we have set out a number of other issues identified within the Reforms, as detailed below:

Issue #	Reference or particulars	Comments
General Issues		
1.	2(1) (no 5) "the Chapter 2G Reforms"	What is this in reference to and how are those "Reforms" different to the ones proposed within the Bill?
2.	No Regulations or Rules provided	Very difficult to do a proper assessment of this legislation without the Regulations or Rules
3.	No guidance or rules about how these Reforms will work with corporate trusts	• 454P ipso facto voiding looks like it will assist • Consider excluding corporate trustees from these Reforms as they don't really fit the simple insolvency eligibility • What if the corporate trustee is trustee of more than 1 trust?
4.	ASIC insolvency practitioner levy	• This **must** be suspended for 1 year at least, if not 3 years or indefinitely • Will the Restructuring Practitioner (RP) also be required to pay the ASIC levy on each Restructuring they perform?
5.	Qualifications to be a Restructuring Liquidator	• Very limited guidance provided to date • The same test as applying to be a Registered Liquidator **must** be adopted • Adopt ARITA's view on same
6.	91 relation back day	• These provisions are almost all correct, except #21 and #22 are the same. We recommend deleting #22
7.	60 18 remuneration	• No framework provided to date, instead left to the unpublished Rules • Remuneration expectations will depend on the scope of the obligations and liabilities of the RP. • If it is anticipated that the RP can only charge a small fixed fee upfront (say less than $5k), the current framework is too burdensome to accomplish this. • It is not expected small business owners will have this kind of cash, so how will this be funded? • **Recommend** the Government give a $10k grant to any company that elects to do this Restructure and Plan for the first 12 months of the Reforms
8.	Page 76 "schedule 2"	• Confusing reference to Schedule 2, when the Corporations Act already has such a schedule. Consider renaming. • No framework provided, which needs to be given urgently for consultation

Issue #	Reference or particulars	Comments
Restructuring		
9.	452A "that allows the companies"	Replace with "it" or "the eligible companies"
10.	453(1)(a) liability threshold eligibility	• Regulations/Rules are to include these details • What about: Contingent or unliquidated claims What are the types of employee entitlements that this applies to Unforeseen liabilities or delays by creditors in issuing invoices Set off claims that bring the amount of creditors below the liability threshold • Will the liability threshold be subject to change each year like the AFSA indexes? • Why do all employee entitlements need to be paid? Very few companies will meet this test. • Why not limit this entitlement test to say 5% of all liabilities as opposed to full payment? • Will unpaid director and related party employee entitlements mean the company does not meet the test? • What about if a restructuring begins during the middle of a pay period? • What if it turns out that employees were previously underpaid and the Plan is in full effect? • Will leave entitlements be included? • Can you make employees redundant or stand them down during the Restructuring or during the Plan? If not, this will hamper the flexibility of the Restructure.
11.	453C(b) prior Restructurings exclusion	• What if the RP or the current director(s) do not know if a past or current director(s) fails this test? • How will they declare this aspect of the eligibility? • Will ASIC searches reveal that a current or past director has failed this test? Is the RP obligated to perform and pay for this search or are the director(s) responsible? • Assuming no director identification number in the early stages of the Reforms, what if the searches do not show the failure of this test? This could be because a director has registrations under multiple different versions of his or her name. Again who is responsible for this? • Can you put a group of related parties into Restructuring at the same time? The provision refers to "has been". • Possible loophole say you have 2 directors, and 1 doesn't meet the test. Could the 1 director that doesn't meet the test, resign on the day of, and immediately prior to, the Restructuring. This is because the provision says "preceding that day"
12.	453D DIRRI	• "as soon as practicable" is an undefined test. Further clarification is needed. As currently defined will require 2 sets of notices to be sent to creditors during the Restructuring, which is only going to increase its cost • Lodging the DIRRI with ASIC not only requires the PDF lodgement but also for the Practitioner to fill out a form. This adds costs. Consider how to reduce this burden. • We suggest providing a specific timeframe and consider how it could be implemented to reduce the reporting burden and costs • DIRRI is incredibly important, but the current precedents required by ASIC are burdensome and difficult to creditors to read and understand. ASIC needs to invest in an appropriate and simple precedent for industry to use. It should be 1 page only
13.	453E "are"	• Consider changing the final word "are" to "include"
14.	453F "attend"	• What does "attend" mean, particularly in a COVID 19 world? • What if the RP only requires a video or telephone attendance? • Replace with "must attend upon a written request of the [RP]" and then give allowance for the RP to prescribe the conditions upon which attendance must be completed
15.	453G receipt of books and records from third parties	• No penalty prescribed for a failure to comply • Bank statement sourcing from Banks is a continued pain for all practitioners, and in some cases requires us to pay a fee to obtain same. This should be prohibited by the Corporations Act • Will specific directions be provided to the ATO and relevant State Revenue Offices that they must provide information to the RP? • Current ATO FOI time period is about 28 days. This needs to be drastically reduced to fit within the time periods prescribed in the Restructuring

Issue #	Reference or particulars	Comments
16.	453J(3)(c)(i) & (4)	• How do you give notice to the company if 109X is being changed to include the office of the RP? • Can the RP simply notify the director and send a letter to its office that it intends to terminate the Restructuring or the Plan?
17.	453L void dispositions	Needs to specify that the burden of proof lies with the Defendant
18.	453L(3)	• This could be open to abuse if a notice of Restructuring does not need to be filed immediately upon appointment of the RP. • Again the provision does not say that the burden of proof lies with the Defendant
19.	453LA(1)(a) "453(1)"	• This is an error and should instead refer to 453L(1) • Who may apply for such an order? • The provision says the money is (inter alia) to be "[paid] … to the company". A Defendant could raise set off in 553C as a defence to this provision, if they are owed monies
20.	453M "good faith"	• Why make this subject to "good faith" if consent of the RP or order of the Court?
21.	453T(1)	• Why only written notice, and not also the resolution lodged with ASIC? • Treasury should adopt the wording in 453L(3)(c) instead
22.	459P ipso fact restriction	• This is an important provision and we commend Treasury for its inclusion • What about QBCC licence restrictions? Will the Restructuring or Plan trigger an insolvency event for a construction company in QLD? If so, and if not restricted, then construction companies in QLD would not be able to use the Restructuring or Plan
23.	456H	This works, but only if the RP is appropriately qualified, experienced and licenced just like a current registered liquidator (RL)
24.	456B(3) & Schedule 3	The penalty unit (PU) for a person that acts as an RP but is not a RL is only 50 PU or c$10k. A higher PU needs to be considered to protect the integrity of these Reforms
Small Liquidation		
25.	Requirement that all tax returns and BAS's must be lodged	• In our experience, very few companies will meet this test at the time they intend to commence a creditors voluntary liquidation (CVL). It is a very limiting eligibility requirement that should be abolished or nuanced • There is no or limited incentive here for a director to comply with these lodgement requirements just so that the small liquidation (SL) can be used. They are unlikely going to want to spend their own money to get lodgements up to date, if they are not going to get anything out of it • Consider nuancing this requirement with further exceptions and examples.
26.	Must only be creditors voluntary liquidation(CVL), and not members voluntary liquidation (MVL) or court liquidation (CL)	• Agree that this should not apply to an MVL • Strongly disagree that the SL not apply to a CL. It limits the companies that will actually be able to use the SL even further • Consider including CL's where the RL elects to use the SL within the timeframes required by the Bill
27.	500AE(2) CVL normal vs SL exclusions	• Unable to identify where the actual costs savings are, other than maybe a couple of thousand dollars by not having to do a 533 • Still required to issue 2 cumbersome reports to creditors and deal with all of the employee and creditor issues that go with a normal CVL • Treasury must release its modelling on what cost savings they are expecting here
28.	498(2)(a) & 500A(2)(a) and initial first report to creditor timeframe	• The timeframe works to give notice to creditors of the SL intention, but need to make sure that it fits in with the date of the first report to creditors being due • Otherwise may have to send out 2 reports in the first month • Consider changing 498(2)(a) to "… up to 10 business days after …"
29.	500AA(1)(e) DIRRI	Same issue as #12 above
30.	500AB	• What purpose does this serve? • Consider deleting

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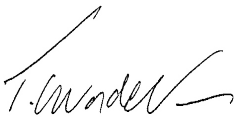
This submission has been prepared and approved on behalf of SV Partners by the below signatories.



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About SV Partners

SV Partners is an expert accounting and specialist advisory firm focused on supporting businesses and individuals in financial stress.

SV Partners has been working with small to medium businesses across industries to help with financial stress for over 17 years. We work hard to ensure the best possible outcome by carefully considering the full circumstances, addressing concerns and providing tailored solutions.

Every situation is different and our team ensures that clients understand all of the options available to them in navigating through financial stress.
We deliver superior outcomes by focusing on exceptional service delivery, respecting our clients, exceeding their expectations and working effectively as a team.

National Strength with Regional Capability

SV Partners is a national practice represented across Australia by a team of over 150.

In addition to our metro offices, SV Partners maintains a strong regional focus in QLD and NSW with offices in Mackay, Rockhampton, Sunshine Coast, Toowoomba, Gold Coast, Wollongong, Newcastle, Dubbo and Tamworth.

Our experience has allowed us to develop expert skills and apply them across small and large scale matters across industries.

Our Offices

SV Partners is a specialist accounting and expert advisory firm focused on supporting professionals and their clients.

We provide professional corporate and personal insolvency accounting, turnaround strategy advice, forensic and advisory services to accountants, financial institutions, corporations, financial and legal advisors, and their clients. SV Partners are the professional's proven partner.

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