



24 November 2020

Manager
Market Conduct Division
Treasury
Langton Crescent
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By email MCDInsolvency@Treasury.gov.au

Dear Sir / Madam

Insolvency reforms to support small business – subordinate legislation

We note the release of the exposure drafts of the Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020 (Draft Regulations), the Corporations Amendment (Corporate Insolvency Reforms) Rules 2020 (Draft Rules) and the associated explanatory memoranda.

The ABA provided a submission on the Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (Bill), and we welcome the opportunity to provide feedback on the Draft Regulations and Draft Rules, while noting our comments below on the timeframe for the implementation of this regime generally.

Our feedback on the Draft Regulations and the Draft Rules is underpinned by the same principle as our feedback on the Bill: we are supportive of the aims of the Corporate Insolvency Reforms and encourage focus on achieving an appropriate balance for creditor protections. This principle is relevant not just for banks but also, and more particularly, small business creditors who will be impacted by the Corporate Insolvency Reforms. To that end, we reiterate our comments and feedback in our previous submission and make the following comments and suggestions with respect to the Draft Regulations and Draft Rules.

Key Points

- The Government should commit to a review of the new regime at an appropriate stage after it takes effect
- Restructuring plans should allow for a maximum of 1 to 2 years for the company to make repayments, rather than the proposed maximum 5 years
- The Draft Rules should provide for a clear mechanism for reporting behaviour which is not consistent or not perceived to be consistent with the intended aims and terms of the Bill, the Draft Regulations or the Draft Rules. This could include an easy to use reporting hotline and database to record reports and findings maintained by the regulator.
- There are some respects in which the exposure drafts would benefit from clarification – either in the documents themselves or, potentially, in the explanatory material. These are set out in detail below

Post implementation review

We note at the outset that the time allowed for consultation on the Bill, as well as the regulations and associated documents, is very short and the planned commencement on 1 January 2021 leaves little time for creditors, debtors and practitioners to prepare for the new regulatory environment.



We therefore think it would be useful for the Government to undertake a review of the operation of the new laws, perhaps two years after the date that they take effect.

Small business

As noted in the Explanatory Memorandum to the Regulations, the intention of this regime is to create “a system of external administration that can accommodate the needs of *small businesses*”. To this end the new debt restructuring regime is subject to a threshold of \$1 million in a business’ total liabilities.

While we support that threshold amount, and making the regime accessible to small businesses, in our view, it should not be open for businesses that are, in substance, large, complex or sophisticated businesses, to avoid the threshold. This could be the effect, for example, where businesses within a large corporate group are assessed on their own liabilities in isolation – not taking account of the total liabilities of a group of which they are part.

On the current drafting of section 435C of the Act, and the \$1 million threshold in the regulations, this would seem to be the effect.

In our view, the Government should consider whether this appropriately reflects the policy intent - to limit access to the new restructuring process to *small* businesses.

Restructuring plan payment period

Under regulation 5.3B.13(4)(b) a restructuring plan may provide for payments to be made for a period of up to 5 years. Given the aim of the restructuring process is to effect an expedited restructuring of small business this period is too long. The expectation is that small businesses utilising the restructuring process will have relatively simple debt structures and simple assets to be realised to satisfy those debts. Such assets should be capable of being realised within a short period of time. The restructuring period should reflect the aim of quickly restructuring small business.

Under existing comparable regimes – voluntary administration and deeds of company arrangement - timeframes for repayment are usually much shorter than 5 years. The restructuring plan should allow for payments over a period of no more than 1 to 2 years. The longer a restructuring plan is in place, the longer uncertainty about the business’s financial capacity will remain, restrict its access to capital and allows for costs to be incurred. The proposed period of up to 5 years does not appear consistent with the aims of the new process.

Complaints and reporting poor outcomes

The Draft Regulations and Draft Rules have provided avenues for creditors to dispute or challenge a restructuring plan. We support these measures. These are important mechanisms for ensuring the validity of the restructuring process. However, undertaking a challenge will often require legal challenge requiring court orders.

We are concerned that pursuing such a course of action is both costly, time consuming and complex. These factors may dissuade small business creditors from pursuing action. This is particularly so given the context of a small business creditor’s claims against a debtor being compromised as a result of a restructuring plan and the financial distress this may cause for a small business creditor. The cost, time and complexity could act a significant barrier to these important validity measures.

To address this, the Draft Rules should provide for a clear mechanism for reporting behaviour which is not consistent or not perceived to be consistent with the intended aims and terms of the Bill, the Draft Regulations or the Draft Rules. This would include an easy to use reporting hotline and database to record reports and findings maintained by the regulator.

Statement of Debts and Claims

The Statement of Debts and Claims will be relevant to determining which debts and claims will be effected by the restructuring plan as well as calculating value for voting. Ensuring that all creditors have



an opportunity to consider and, if appropriate, challenge the Statement of Debts and Claims will be fundamental to ensuring creditor certainty and support for the restructuring plan and new process.

The Draft Regulations provide a period of 5 Business Days from a creditor receiving the restructuring plan or becoming aware of the restructuring to notify the restructuring practitioner that it disputes the Statement of Debts and Claims. Some ABA members have questioned whether this period is sufficient for secured creditors to receive, process and report on the Statement of Debt and Claims.

In our view, the Government could consider whether a period of 10 business days would represent more adequate timeframe for a secured creditor to confirm the accuracy of the information contained in the statement, as well as collate any information necessary to dispute the Statement.

Points that require clarification

Some members have expressed the view that the exposure drafts could benefit from clarification in some respects. This could be achieved either in the documents themselves or, potentially, in the explanatory material. We discuss these below.

Valuation

The Draft Regulations provide that a Secured Creditor will receive payment under the restructuring plan to the extent that its debt or claim exceeds the value of its security (regulation 5.3B.25). The admissible debt will also be relevant for the extent to which a Secured Creditor is bound by the terms of a restructuring plan (if it is approved by the creditors) (regulation 5.3B.27(3)).

The ABA understands that secured asset valuations will be conducted under existing laws and practices based on the secured creditor's assessment of the asset's value.

Effect on Creditors

The Draft Regulations provide the detail of what will need to be included in a restructuring plan, however, it does not consider how debts and claims will be treated once the restructuring plan is made or where all the obligations under the plan have been completed.

Some members have expressed the view that it is not clear how interest will be treated for debts that continue to accrue during the restructure period or the period of the restructure plan. For example, overdrafts available to small businesses would be expected to continue during the restructuring plan.

We would expect that the debts and claims of affected creditors who are bound by the restructuring plan will be released up to the date the restructuring commences. A similar approach has been taken in respect of debt agreements under the Bankruptcy Act and similar terms could be incorporated and would be consistent with contingent liabilities not being admissible debts and not being effected by the restructure plan.

Effect on Secured Creditors

Under the Draft Regulations a Secured Creditor will be bound by a restructuring plan to the extent they agree to be bound or accept the proposal (regulation 5.3B.27(3) and (4)).

Some members consider that it is not clear what is required for the secured creditor to agree to be bound, and it is also not clear the extent to which its debt or claim will be affected by the restructuring plan.

A sensible outcome would be that:

1. a secured creditor agrees to be bound either expressly in writing or otherwise by voting for the restructuring plan; and
2. if the secured creditor is to be bound by the restructuring plan, that a secured creditor's debt or claim will only be affected by the restructuring plan to the extent of the admissible debt ie the



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Secured Creditor's whole debt or claim will not be compromised by the restructuring plan.
Regulation 5.3B.30(2) should reflect the approach described in regulation 5.3B.27(3).

Confirmation that this is the intent would be useful.

Please let me know if you'd like to discuss any of the above matters.

Yours sincerely

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