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Public Submission

Dear Sir/Madam

Consultation: Increasing the Statutory Demand Threshold

We thank you for the opportunity to make a submission in response to Treasury's consultation on whether to permanently raise the monetary threshold at which creditors can issue a statutory demand on a company.

Over 96% of Australian registered proprietary companies are small businesses. Accordingly, ASIC's submission focuses on the potential impact of a change in the statutory demand threshold on those businesses from both sides of the supply chain.

ASIC has no data on statutory demands that would enable us to comment on the likely impact on business (particularly small business) of increasing the monetary threshold at which creditors can issue a statutory demand to a specific higher amount. Further, ASIC has no information to enable us to comment on the extent to which the current statutory demand process is being used by small businesses (as opposed to banks or Government departments) to support their management of credit risk in their customers.

ASIC acknowledges that the current amount of $2,000 has been in place since at least 1992, and in real terms without CPI increases may not reflect its original intent.

We respond to each of the questions proposed in the consultation paper. Our comments on Questions 1 and 2 are dealt with together.

Question 1: Should the threshold at which a statutory demand can be issued on a company be increased?
Question 2: If the threshold is increased, to what amount should it be increased and why?

As noted in the consultation paper, "*the central function of a statutory demand is to establish proof of a company's inability to pay its debts. It does so by creating a rebuttable statutory presumption of insolvency where a company fails to respond to a demand that has been served upon it*."

In effect; failure to comply with a statutory demand helps suppliers avoid the additional cost, and overcome the difficulty of establishing a company's insolvency, making it easier to pursue recovery of amounts legitimately owed to it by a debtor. It also provides an effective mechanism for a business to manage its customer insolvency risk.

Any change to the statutory threshold must be considered together with the aims of the recently enacted small business insolvency reforms to facilitate small business restructure.

Increasing the monetary threshold at which creditors can issue a statutory demand may contribute to the inefficient allocation of scarce resources through:

- increasing the barriers for suppliers of credit to recover amounts legitimately owed to them to help sustain and grow their own (viable) businesses; and
- enabling poorly performing and unviable businesses to continue to operate.

If Government determines that an increase to the monetary threshold at which creditors can issue a statutory demand on a company is appropriate, the following factors might be considered:

- setting the threshold amount at a level most viable small businesses can pay. This would avoid unnecessary liquidation of a company
- not setting the threshold too high so it acts as a disincentive for directors to seek advice and act early to restructure the company
- not setting the threshold so high that the additional cost of pursuing recovery of the debt makes doing so prohibitively expensive for small business
- setting the threshold amount at a level most viable small businesses can sustain as a supplier, avoiding unnecessary pressure and increased debt on supplier companies.

Imposing a fee to issue a statutory demand, similar to the fee in personal insolvency to issue a bankruptcy notice, may mitigate against a statutory demand being used as "*a debt recovery tool to coerce a company into paying a disputed debt*" as mentioned in the consultation paper.

Alternatively, if Government is minded to significantly increase the amount, consideration might be given to increasing the time to respond to a statutory demand before winding up proceedings can be commenced.

ASIC notes the threshold amount to issue a bankruptcy notice under the Bankruptcy Act 2001 was increased in January 2021 from $5,000 to $10,000.

Less than 30% of personal insolvencies in the September 2020 and December 2020 quarters were of debtors involved in a business (i.e. as a sole trader or the debtor was a director, secretary or held a management role in a company (possibly as an employee)). We understand most personal insolvencies involve 'consumer' debtors where many creditors are financiers (home/personal loans and credit cards), utilities (power, water and telecommunications) and other statutory authorities (council rates etc). If correct, few creditors in these bankruptcies are other small businesses which are most likely to be impacted by the monetary threshold at which a bankruptcy notice can be issued i.e. financiers and utility companies have the cash flow and financial resources to absorb the impact of the raised monetary threshold.

Question 3: If the threshold is increased, when should this change come into effect?

If Government determines that an increase to the monetary threshold at which creditors can issue a statutory demand on a company is appropriate, ASIC is of the view that deferring the effective date of any increase for a period (say six to 12 months) after legislation is passed warrants consideration.

This would provide both the company and suppliers of credit an opportunity to review, and if necessary, renegotiate, the terms of ongoing supply contracts and minimise potential adverse impacts of a sudden change (particularly on small business).

Question 4: What will be the impacts of increasing the threshold?

Setting the threshold amount at a level most viable small businesses can pay would avoid unnecessary liquidation of companies; i.e. increasing the level by a modest amount would avoid unnecessary liquidations.

However, increasing the monetary threshold at which creditors can issue a statutory demand might:

- result in suppliers of goods or services on credit pursuing other options to recover amounts legitimately owed to them – including, declining to supply goods or services on credit terms at all, exercising the right to stop supply, requiring personal guarantees from directors (and others) where none are currently required and increased action against guarantors to recover amounts owed by a corporate customer; thereby impeding small business growth on both sides of the supply chain, and their recovery, post-pandemic

- increase the cost, particularly to small business, of recovering amounts genuinely owed to it, thereby adversely impacting the supply of credit and the viability and growth potential of small business
- permit unviable business to continue to trade or result in increased 'zombie' companies, resulting in the inefficient allocation of scarce resources and impeding economic growth
- not support recent insolvency reforms aimed at encouraging small business to act early and maximise the chances of restructuring their business
- lead to the inefficient allocation of scarce resources as a supplier's ability to pursue amounts owed to it and wind up unviable business is effectively reduced

ASIC would welcome the opportunity to work with Treasury on this important policy issue. Please contact Thea Eszenyi by telephone on (03) 9280 4401, or by email at thea.eszenyi@asic.com.au, if there is any aspect of this submission you wish to discuss further.

Yours faithfully

Greg Yanco
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