The Parliament of the Commonwealth of Australia

# Inquiry into the Exposure Draft of the Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004

**House of Representatives**
**Standing Committee on Legal and Constitutional Affairs**

July 2004
Canberra

ISBN 0 642 78483 3

# Contents

# Membership of the Committee

**Chair** Hon Bronwyn Bishop MP

**Deputy Chair** Mr John Murphy MP

**Members**

Hon Julie Bishop MP
(until 07/11/03)

Hon Alan Cadman MP

Hon Duncan Kerr MP

Mr Daryl Melham MP
(until 11/08/03)

Ms Sophie Panopoulos MP

Hon Con Sciacca MP

Mr Patrick Secker MP

Dr Mal Washer MP

Hon Alexander Somlyay MP
(from 07/11/03)

Mr Robert McClelland MP
(from 11/08/03)

# Committee Secretariat

| | |
|---|---|
| **Secretary** | Gillian Gould |
| **Adviser** | Amanda Pearce |
| **Administrative Officers** | Frances Wilson |
| | Heidi Luschtinetz |

# Terms of reference

The Committee will inquire into the provisions of the draft Bill. Specifically, the Committee will consider whether these provisions adequately address the problems identified in the Taskforce report, namely:

(a) high income earners using bankruptcy to avoid paying debts that they can afford to pay, while continuing to enjoy a lifestyle made possible through the build up of assets in the names of third parties
(b) the uncertainty arising from the interaction between family law and bankruptcy
(c) the inadequacy of the current income contributions scheme in circumstances where a bankrupt chooses not to comply, and
(d) the use of financial agreements to defeat the claims of creditors.

# List of abbreviations

| | |
|---|---|
| ABA | Australian Bankers' Association |
| ACEA | Association of Consulting Engineers Australia |
| AICD | Australian Institute of Company Directors |
| AFCCRA | Australian Financial Counselling and Credit Reform Association |
| AGD | Attorney-General's Department |
| AMA | Australian Medical Association |
| ATO | Australian Taxation Office |
| BLAAAMB 2004 | Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 |
| CPA Australia | Certified Practicing Accountants Australia |
| The FLS of the LCA | The Family Law Section of the Law Council of Australia |
| ICAA | Institute of Chartered Accountants in Australia |
| The IRC of the LCA | The Insolvency and Reconstruction Committee of the Law Council of Australia |
| IPAA | The Insolvency Practitioners Association of Australia |
| ITSA | Insolvency and Trustee Service Australia |

| | |
|---|---|
| IWIRC | The International Women's Insolvency and Reconstruction Committee Australian Network (Qld) Inc |
| LCA | Law of Council of Australia |
| NIA | The National Institute of Accountants |
| NNWLS | The National Network of Women’s Legal Services |

# List of recommendations

## 2 Overview of the Proposed Bill

**Recommendation 1** (paragraph 2.14)

The Committee recommends that financial agreements revert to the pre-2000 amendments to the *Family Law Act 1975* and be subject to confirmation by the court which shall take into account bankruptcy ramifications.

## 3 Recovery of Property Amendments: Proposed New Division 4A of Part VI of the Bankruptcy Act

**Recommendation 2** (paragraph 3.46)

The Committee recommends that:

- the amendments contained in Schedule 1 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and other Measures) Bill 2004 be abandoned; and
- Insolvency and Trustee Service Australia and the Attorney-General's Department undertake fresh consultation with the Bankruptcy Reform Consultative Forum with a view to strengthening the current clawback provisions in the Act (sections 120 and 121 in particular).

**Recommendation 3** (paragraph 3.47)

The Committee recommends that subsection 16(4) of the *Income Tax Assessment Act 1936* and section 3C of the *Taxation Administration Act 1953* be amended to:

- authorise the Commissioner of Taxation to provide publicly available information to prescribed industry or professional organisations; and
- authorise the Commissioner of Taxation to utilise publicly available information for the purposes of the role of Chief Executive of the Australian Tax Office.

## 4 Bankruptcy and Family Law Amendments

**Recommendation 4** (paragraph 4.22)

The Committee recommends that the amendments proposed in Schedule 2 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 be implemented.

## 5 Supervised Account Regime

**Recommendation 5** (paragraph 5.17)

The Committee recommends that the amendments proposed in Schedule 3 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 be implemented.

## 6 Financial Agreements

**Recommendation 6** (paragraph 6.15)

The Committee recommends that the amendments proposed in Schedules 4 and 5 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 be implemented.

# 1

# Introduction

1.1 The exposure draft of the Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 (BLAAAMB 2004), together with an accompanying draft Explanatory Memorandum, was referred to the Committee on 13 May 2004 by the Attorney-General, the Hon Philip Ruddock MP, for inquiry and report in July 2004.[1]

1.2 The Attorney-General requested that the Committee inquire into the provisions of the draft Bill, considering specifically whether the provisions adequately address problems identified in a Joint Taskforce Report on the *Use of Bankruptcy and Family Law Schemes to Avoid Payment of Tax* (January 2002).

## Joint Taskforce Report

1.3 On 22 March 2001 the (then) Attorney-General, the Hon Daryl Williams AM QC MP, and the (then) Assistant Treasurer, Senator the Hon Rod Kemp, announced the establishment of an inter-agency Taskforce to consider whether any changes should be made to bankruptcy and taxation laws to ensure that bankruptcy is not used as a means to avoid tax obligations.[2]

---

1 The Committee was initially asked to report by 16 July 2004; given the large number of submissions received by this inquiry an extension was sought until the end of July.

2 Joint Taskforce Report on the *Use of Bankruptcy and Family Law Schemes to Avoid Payment of Tax*, Attorney-General's Department, Australian Taxation Office, Insolvency and Trustee Service Australia and Treasury, January 2002, p. 4.

1.4 The Taskforce consisted of officers from the Attorney-General's Department (AGD), Insolvency and Trustee Service Australia (ITSA), the Australian Taxation Office (ATO) and the Treasury.

1.5 The Taskforce identified the problem of a small but significant number of high-income debtors, typically high earning fee-for-service professionals, who use bankruptcy to avoid paying their taxation and other debts:

> These debtors have the ability to pay their debts but instead fund a lifestyle made possible only through the non payment of debts and the build up of assets in the names of related parties. Some such debtors divert income and other assets to other parties in a manner designed to thwart the capacity of the bankruptcy trustee to realise their value for the benefit of creditors. In such cases the return to creditors in a bankruptcy more often reflects the bankrupt's ability to structure their affairs in a certain way rather than their substantive or real wealth.[3]

1.6 This scheme only worked because the professionals concerned could continue to work in their professions as an undischarged bankrupt. Some barristers had failed to lodge tax returns at all, or for many years had failed to file.

1.7 The problems identified by the Taskforce formed the basis of the Terms of Reference for this inquiry:

(a) high income earners using bankruptcy to avoid paying debts that they can afford to pay, while continuing to enjoy a lifestyle made possible through the build up of assets in the name of third parties

(b) the uncertainty arising from the interaction between family law and bankruptcy

(c) the inadequacy of the current income contributions scheme in circumstances where a bankrupt chooses not to comply, and

(d) the use of financial agreements to defeat the claims of creditors.

3 Letter, Attorney-General to the Hon Bronwyn Bishop MP, dated 13 May 2004.

1.8 The Taskforce made a number of recommendations for amendments to relevant Commonwealth legislation and administrative practices but the concept of 'tainted property' was not canvassed by the Taskforce. The original concept which was canvassed in recommendation 3 of the Taskforce Report was found to be unconstitutional.

1.9 The Attorney-General stated that the amendments proposed by the draft Bill are intended to address the issue of high income professionals using bankruptcy as a mean of avoiding their taxation and other obligations:

> In particular, the amendments will provide creditors with improved access to assets which are substantively those of the bankrupt but which are held in the names of other entities (such as the bankrupt's spouse or another family member). The amendments will also address longstanding issues concerning the interaction between bankruptcy and family law which have created uncertainty as to the competing rights of creditors and a bankrupt's spouse.[4]

1.10 The amendments proposed in the draft Bill would implement a number of the Report's key recommendations relating to the *Bankruptcy Act 1966* (the Act) and the *Family Law Act 1975* (the Family Law Act). There was nothing in the exposure draft of the proposed Bill to indicate the targeting of high income professionals. Evidence showed that the application would dramatically affect "ordinary punters" and have far reaching applications.

## The Committee's Inquiry

1.11 The Committee advertised the inquiry nationally and sought submissions from interested individuals and organisations.[5]

1.12 The Committee received over 180 written submissions and held public hearings in Canberra on 5 and 6 July and in Sydney on 22 July 2004.[6]

---

4 Letter, Attorney-General to the Chairman, the Hon Bronwyn Bishop MP, dated 13 May 2004.

5 The inquiry was advertised in *The Australian* on 19 May 2004 and placed on the Committee's website.

# General Observations

1.13 The Committee found general agreement that measures should be implemented to address the deliberate use of bankruptcy laws by high income earners to avoid tax and other debts. It also found that the ATO had been derelict in its duty in failing to identify tax defaulters, namely barristers who abused the bankruptcy laws to avoid paying tax.

1.14 However, 98% of the more than 180 submissions to the inquiry opposed the proposed amendments to the Act, whereby Division 4A of Part VI is proposed to be replaced with a new Division 4A.

1.15 The schedules relating to amendments to the Family Law Act in evidence were generally agreed with, or the submissions were silent.

## Process of Consultation

1.16 Mr Ian Gilbert from the Australian Bankers Association stated that an edited version of the Joint Taskforce Report was made available to members of the Bankruptcy Reform Consultative Forum. The forum consists of representatives of the finance industry, lawyers, insolvency practitioners and includes a financial counsellor.[7] According to Mr Gilbert the forum:

> ..has been looking at this proposal for some 15 months or more. There is… a level of concern from a majority of people on that forum that the bill is missing the mark.[8]
>
> …the majority of the members on the forum were not supportive of tackling that problem in the way that is being proposed.[9]

1.17 However what was in the exposure draft was not part of this process.

1.18 The Committee understands that issues papers were prepared in November 2002 and July 2003 for consideration by the consultative

---

6 Appendix A contains a list of submissions, Appendix B contains a list of exhibits, Appendix C contains a list of witnesses at public hearings and Appendix D contains a list of Federal Court and Federal Magistrates Court cases where sections 120 and 121 of the Act have been considered (from 2000-2004).

7 ABA, *Transcript of Evidence*, 5 July 2004, p. 86.

8 ABA, *Transcript of Evidence*, 5 July 2004, p. 81.

9 ABA, *Transcript of Evidence*, 5 July 2004, p. 86.

forum.[10] Notwithstanding ongoing resistance from members of the forum draft legislation was developed to address the problems identified by the Joint Taskforce.[11]

1.19 ITSA advised that in September 2003 advice was sought from the Australian Government Solicitor on constitutional issues and found some elements of the proposed legislation to be unconstitutional.[12]

1.20 A revised proposal was developed in December 2003 and considered by the consultative forum.

1.21 Consultation with the Bankruptcy Reform Consultative Forum occurred on three further occasions prior to the release of the exposure draft currently under consideration by this Committee. Mr Bergman advised:

> Shortly after the government made its announcement, we had a meeting of the consultative forum to explain the changes but not to discuss them. We convened a workshop on 4 February 2004, following a desire expressed by the forum members at the December meeting, to present and consider an early draft of this legislation. We spent the best part of the day discussing it with the parliamentary drafters present. On 9 March we had another meeting of the consultative forum, at which we talked at a fairly general level about some possible further changes, which have now been reflected in the exposure draft.[13]

1.22 The Committee found that the 'further changes' discussed at the March meeting included the introduction of the concepts of 'tainted purpose', 'tainted property' and 'tainted money'.[14]

## 'Tainted purpose', 'tainted property' and 'tainted money'

1.23 The Committee was advised that central to the proposed amendments are the concepts of a 'tainted purpose', 'tainted property' and 'tainted money'.

1.24 The Committee notes that the concepts of 'tainted purpose', 'tainted property' and 'tainted money' are new concepts within bankruptcy

10 ITSA, *Transcript of Evidence*, 6 July 2004, pp. 25 – 29.
11 ITSA, *Transcript of Evidence*, 6 July 2004, p. 26.
12 ITSA, *Transcript of Evidence*, 6 July 2004, p. 27.
13 ITSA, *Transcript of Evidence*, 6 July 2004, p. 28.
14 ITSA, *Transcript of Evidence*, 6 July 2004, p. 28.

legislation. The originators of the concepts stated that they were unaware of them existing in any other jurisdiction.

1.25 The Committee is concerned that, given that the concepts are central to the proposed amendments to Division 4A, they were not central to the consultation process.

# 2

# Overview of the Proposed Bill

2.1 This chapter sets out the main elements of the proposed Bill, with respect to:

- recovery of property;
- interaction between family law and bankruptcy;
- collection of income contributions; and
- family law agreements.

## Recovery of Property

2.2 The draft Bill proposes to replace the existing Division 4A of Part VI of the Act with a new Division which will allow trustees in bankruptcy to recover property held by third parties / entities where:

- the property was acquired by a third party / entity using funds or property provided by the bankrupt;
- the bankrupt's purpose in making that transfer was to ensure that the funds or property would not be available to pay creditors; and
- the bankrupt has used or derived a benefit from the property now held by the third party (including any replacement property which can be traced to the original transfer).

2.1 The provisions will not apply where the third party provided market value consideration in return for the original transfer and the transfer occurred more than 10 years prior to the bankruptcy. Nor will they

apply where the third party provided market value consideration in return for the original transfer and, where the transfer occurred less than 10 years prior to bankruptcy, the transferee was unaware of the bankrupt's purpose in making the transfer. However a reverse onus of proof applies.

2.2 The Explanatory Memorandum describes the policy underlying these proposed changes:

> The amendments proposed by this Bill are intended to address the issue of high income professionals using bankruptcy as a mean of avoiding their taxation and other obligations. In particular, the amendments will provide creditors with improved access to assets which are substantively those of the bankrupt but which are held in the names of other entities (such as the bankrupt' s spouse or another family member).[1]

2.3 The Explanatory Memorandum also notes that, while they may impact on arrangements commonly used by professionals and business people, the proposed changes represent a 'shift' in Government policy:

> Arrangements of the type which are potentially within the scope of the new provisions are not uncommon. Many professional people consider such arrangements to be a legitimate way of arranging their affairs to protect some of their personal wealth from claims which arise as a result of their professional activities. For professionals who are required to practise in their own name (that is, who are not allowed to incorporate), these arrangements may be seen as providing protection comparable to that given to a corporation.
>
> The amendments proposed by this Bill represent a fundamental shift away from the perceived legitimacy of these arrangements. Although the arrangements may continue to be legitimate for other purposes, the Government does not believe that these assets should remain protected where creditors' claims cannot be met from assets held in the bankrupt's name whilst the bankrupt continues to enjoy a lifestyle effectively funded by his or her own means. The

1 BLAAAMB 2004 Explanatory Memorandum, p.3.

> bankruptcy system should not be the means by which a person can protect his or her wealth from business failure whilst creditors bear all the risk associated with that failure.[2]

2.4 It has been stated that such individuals should rely on insurance for protection. Evidence given shows this is not a viable option.

2.5 The proposed amendments can result in the shifting of risk from creditors to the family of the debtor which is effected by elevating the status of the creditor to the same level or better than the family of the debtor. This highlights competing public policies between the aim of the *Family Law Act 1975* to look after children, and that of bankruptcy law which is to look after the interests of creditors. These aims are in conflict in the exposure draft.

## Interaction between Family Law and Bankruptcy

2.6 The Bill also contains amendments dealing with the interaction between family law and bankruptcy. The Explanatory Memorandum refers to the 'difficulties' that can arise when bankruptcy and family law proceedings exist at the same time:

> There are inconsistencies between family law and bankruptcy law which create uncertainty for all involved and can cause hardship for either or both of the creditors and non-bankrupt spouse.
>
> From a bankruptcy perspective, trustees can find themselves in an uncertain position when having to resolve or reconcile competing claims. Creditors unaware of the potential property interest of a non-bankrupt spouse also suffer from a lack of certainty.
>
> From a family law perspective, the legal ownership of property does not always reflect the non-financial contribution of the parties to the marriage. The special interest of the non-bankrupt spouse in the marital property created through both financial and non-financial contributions, which may be recognised by the Family Court in exercising its discretion to alter property interests, is not expressly recognised under the Act.

---

2 BLAAAMB 2004 Explanatory Memorandum, p. 4.

> Different outcomes presently arise depending upon the order in which events occur (those events including separation, bankruptcy and distribution of property by the trustee in bankruptcy).[3]

2.7 The Bill proposes to clarify the rights of the trustee in bankruptcy and the non bankruptcy spouse in these circumstances by, generally, enabling concurrent bankruptcy and family law proceedings to be brought together (see Chapter 4).

## Supervised Account Regime

2.8 The Bill proposes to introduce a supplementary income collection regime (a 'supervised account regime') which will allow the bankruptcy trustee, in certain circumstances, to have access to all the bankrupt's income before it reaches the bankrupt.

2.9 The Explanatory Memorandum describes the perceived inadequacies of the current income collections regime and the general intent of the proposed change:

> Where a bankrupt is employed and has been assessed as liable to pay contributions from his or her income, the Official Receiver can issue a notice to the employer garnisheeing the bankrupt's wages to collect the amount assessed. The Official Receiver can also issue a garnishee notice to a bank or other financial institution to collect contributions.
>
> Some bankrupts (including some high-income professionals) are not 'employed' as such and do not operate bank accounts in their own names. The existing contribution collection scheme is not effective in these cases where the bankrupt chooses not to comply.
>
> These deficiencies will be addressed by the supervised account regime to be introduced by this draft Bill. The amendments will allow the trustee to have access to all of the bankrupt's income before it reaches the bankrupt. This will enable the trustee to use the existing methods for collecting income contributions by ensuring that the bankrupt operates

3 BLAAAMB 2004 Explanatory Memorandum, p.4.

a bank account (into which all income must be deposited) under the trustee's supervision.[4]

## Family Law Agreements

2.10 The draft Bill also proposes amendments dealing with the use of financial agreements under Part VIIIA of the Family Law Act prior to bankruptcy. One amendment will exclude binding financial agreements from the definition of "maintenance agreement"' to allow the trustee to use the Act's "clawback" provisions to recover property transferred prior to bankruptcy pursuant to such an agreement.

2.11 A further amendment will introduce a new act of bankruptcy which will occur when a person is rendered insolvent as a result of assets being transferred under a financial agreement – this will mean that the person's bankruptcy will be taken to have commenced at the time of that transfer which will extend the "relation back" period. This will allow the trustee to claim property transferred under the agreement as divisible property in the bankrupt's estate.

2.12 The committee noted that prior to amendments in 2000 all financial agreements had to be sanctioned by the Court. This requirement was removed in 2000.

2.13 The Committee is of the view, however, that financial agreements should revert to the pre-2000 amendments to the *Family Law Act 1975*.

### Recommendation 1

2.14 **The Committee recommends that financial agreements revert to the pre-2000 amendments to the *Family Law Act 1975* and be subject to confirmation by the court which shall take into account bankruptcy ramifications.**

4 BLAAAMB 2004 Explanatory Memorandum, pp. 4-5.

# 3

# Recovery of Property Amendments: Proposed New Division 4A of Part VI of the Bankruptcy Act

## Outline of Chapter

3.1 In this chapter of the report the following issues are considered:

- Support for the proposed change.
- Criticism of the proposed change, namely that it-
  - ⇒ is a disproportionate response;
  - ⇒ will unfairly impact on asset protection arrangements;
  - ⇒ is retrospective;
  - ⇒ places an onerous burden on asset owners by reversing the onus of proof; and
  - ⇒ is unconstitutional.
- Suggested alternatives to the proposed change, including to-
  - ⇒ make no change to the current Act;
  - ⇒ strengthen the existing claw back provisions in the Act, in particular s120 and s121 of the existing Act; and
  - ⇒ specifically target tax avoiders who become bankrupt.
- The Committee's concerns in relation to the proposed change.
- The Committee's conclusion and recommendations.

# Background

3.2 Current Division 4A of Part VI was introduced into the Act by virtue of the *Bankruptcy Legislation Amendment Act 1987*. The provision allows the trustee to obtain property in certain circumstances from an 'entity' that was 'controlled' by the bankrupt and benefited from his or her 'personal services'. The purpose of the provision is to allow the trustee to recover a bankrupt's property in the situation where that property is disguised as an asset of a trust, company or the like.[1]

3.1 The Bill proposes to substitute this Division with a new Division 4A of Part VI. Central to the proposed amendments are the concepts of a 'tainted purpose', 'tainted property' and 'tainted money'. The 'Simplified Outline' in section 139AA of the Bill describes the key features of the proposed new Division:

> This Division enables the Court to make an order for the recovery of the whole or a part of tainted property, or tainted money, held by an entity other than the bankrupt.
>
> Tainted property is:
>
> (a) property wholly or partly funded by money paid to the entity by the bankrupt before the date of the bankruptcy, where the bankrupt had a tainted purpose in paying the money and the bankrupt used or derived a benefit from the property; or
>
> (b) property transferred to the entity by the bankrupt before the date of the bankruptcy, where the bankrupt had a tainted purpose in transferring the property, the transfer was not made for full value and the bankrupt used or derived a benefit from the property; or
>
> (c) property or money held by the entity as a result of personal services supplied by the bankrupt to or for or on behalf of the entity, where the bankrupt did not receive arm's length remuneration for those services and (in the case of property) the bankrupt used or derived a benefit from the property; or
>
> (d) property or money held by the entity as a result of a scheme entered into or carried out for a tainted purpose, where (in the case of property) the property was not acquired for full value and the bankrupt used or derived a benefit from the property.

1 Bankruptcy Legislation Amendment Bill 1987 Explanatory Memorandum, p.114.

Tainted money is:

(a) money paid to the entity by the bankrupt before the date of the bankruptcy, where the bankrupt had a tainted purpose in paying the money; or

(b) money that represents the proceeds of the disposal of tainted property.

Each of the following is a tainted purpose:

(a) to prevent the property or money from becoming divisible among the bankrupt's creditors; or

(b) to hinder or delay the process of making the property or money available for division among the bankrupt's creditors.

In considering whether to make an order for the recovery of the whole or a part of tainted property or tainted money, the Court must have regard to various matters, including:

(a) the contribution (whether financial or non-financial) of the bankrupt and the entity; and

(b) in the case of property— the extent to which the bankrupt used or derived a benefit from the property.

## Support for the Recovery of Property Amendments

3.2 Only three submissions, including the submission from ITSA, expressed support for the proposed new Division 4A of Part VI. However, a recurring theme in submissions was support for the intent underlying the proposal. The following comments were typical:

> AFCCRA strongly supports the Attorney's intention in this Bill to address the issue of high income professionals using bankruptcy to avoid taxation and other obligations. We believe that any abuse or perceived abuse of bankruptcy brings it into disrepute and makes its appropriate use as a last resort for indebted Australians more difficult.[2]

> AICD strongly supports the stated policy objectives of the Bill set out in the Explanatory Memorandum, namely, to, address the issue of high income professionals using bankruptcy as a means of avoiding their taxation and other obligations. AICD also supports solutions aimed at addressing the identified

2 AFCCRA, *Submission 86*, p.1.

> 'problem' of a small but significant number of high-income debtors, typically high earning fee-for-service professionals, who use bankruptcy to avoid paying their taxation and other debts.[3]
>
> IWIRC supports the objects of the BLAB, particularly with respect to "people who have deliberately and knowingly set about to avoid being able to contribute to their legal obligations using bankruptcy and putting their assets beyond the reach of creditors".[4]

## Criticisms of the Recovery of Property Amendments

3.3 While the evidence suggested a significant degree of support for its policy objectives, the overwhelming number of submissions were critical of the proposed new Division 4A of Part VI. Criticism of the proposed amendment took a number of forms:

- that the proposal is a disproportionate response to the concerns of the ATO as a creditor;
- that the proposal will have unintended consequences for individuals who have legitimately structured their affairs to protect family assets;
- that the retrospective effect of the proposal is a 'draconian' consequence;
- that placing the onus of proof on the respondent entity will create an unfair and onerous burden; and
- that the proposal is potentially unconstitutional.

### A Disproportionate Response

3.4 A number of submissions raised as an issue that the proposed change was a 'disproportionate response' and a 'blanket solution' to address the particular concerns of the ATO. In its submission, the Insolvency and Reconstruction Committee (IRC) of the Law Council of Australia (LCA) asked the question 'Are high income professionals causing a

3 AICD, *Submission 54*, p.1.

4 IWIRC, *Submission 80*, pp.1-2.

"Black Hole" in ATO revenue through bankruptcy?' and provided the following comments:

> It is submitted that the loss of tax revenue, as a percentage of all claims provable in a bankruptcy does not warrant the wholesale changes being proposed…The reforms are not being introduced because of any widespread community concern but because of the concerns of a minority stakeholder.[5]

3.5 Comments in a similar vein included:

> Any attempt by the Government to reform the bankruptcy laws in a general way to specifically aid the ATO to recover tax debts must properly take into account the implications blanket reform would have on small and large businesses, corporate activity and the Australian economy.[6]

> The Bill is an overreaction to the perceived inability of one creditor, the Australian Taxation Office ("ATO"), to undertake effective recovery action against tax evaders or recalcitrant debtors. Instead of dealing with the ATO's problem with targeted, specific legislation or by exploring existing mechanisms, a blanket solution has been proposed with indiscriminate effect and apparently without due consideration being given to the ramification of such a solution.[7]

## Impact on Asset Protection Arrangements

3.6 The overwhelming majority of submissions contended that, as its provisions would allow the trustee to recover assets that had never been owned by the bankrupt, or that had been transferred by the bankrupt many years previously, the proposal would undermine the ability of professionals and business people to protect assets for the benefit of family members:

> Many people structure their affairs to protect their assets for the benefit of their family against the wrongdoing of others. These are people who operate in partnership and therefore are jointly and severally liable for their partner's activities. If

5 The IRC of the LCA, *Submission 98,* p. 17.

6 Arnold Bloch Leibler, *Submission 97,* p.3.

7 Professions Australia, *Submission 81,* pp. 1-2.

> their partner is held to be negligent they will also be liable even though they have not been personally negligent or even knew of their partner's negligent activities. In order to protect their family assets against claims the assets are often not held in the individual's name.
>
> It is no argument to say these people can achieve the same result by operating through a company because in many instances they are legally required to operate in partnership and not in a company. The fact that the Bill operates retrospectively, with no retrospective time limit, significantly compounds the issue.[8]

3.7 A number of organisations gave examples to demonstrate the potential impact of the proposed changes on small business generally:

> Suppose you have a hypothetical situation of a career public servant who might have worked for 30 years. The public servant built up a reasonable nest egg and decided to resign and start off a small business. In that circumstance it is quite reasonable or quite prudent for the wife, for instance, to own the assets, whereas the husband might go off and enter into the business venture which may be of some risk. In those circumstances, the wife can never be properly protected in terms of the husband's future business venture if these amendments were to come through unaltered.[9]

3.8 A related issue raised in submissions was the perceived necessity of asset protection arrangements given the inability of many professionals to adequately insure against risk:

> The AMA strongly believes that individuals and businesses should carry appropriate insurances, however, it is simply not possible to insure against all potential risks. World-wide problems for the insurance industry have seen the rationalisation of policies and small businesses and professionals have found it extremely difficult to access affordable insurance cover for some activities.[10]
>
> Insurance is not always available, and even if it is, there is no guarantee it will cover the risks encountered or be available.

8 National Tax & Accountants' Association Ltd, *Submission 83,* p.1.

9 Pitcher Partners, *Transcript of Evidence , 5 July 2004,* pp.66-67.

10 AMA, *Submission 77,* p.6.

> There is also the issue of HIH Insurance that failed not so long ago and left people with exposures.[11]

3.9 A further issue raised by submitters was that, as a result of their impact on legitimate asset protection arrangements, the proposed changes would adversely impact on risk taking and entrepreneurial activity:

> Professionals and business people who take risks are likely to reduce their exposure to risk and this will have a direct impact on people wanting to go into business and employ people. This will have a direct impact on employment and GDP over time.[12]

3.10 This criticism of the proposed new Divisions 4A of Part VI was also raised by groups other than business and profession organisations. The potential impact of the proposed new Division 4A of Part VI on arrangements designed to protect assets from the consequences of a gambling addiction was raised as an issue by AFCCRA:

> We do see a small number of clients where there may be a gambling problem, for instance, where there is property. The family home may be put into the name of the non-gambling spouse as a means of protecting it and also as a means of confirming that, in fact, the gambler has used their share of the family property, so to speak, in their gambling activity. That could be impacted by some of the provisions of this Bill, and that is a concern to us.[13]

3.11 A related concern was that the proposed change was directed at 'high income professionals' but would potentially impact on individuals generally:

> In Master Builders view, the Bill would also have significant impact on the existing financial arrangements of small businesses, not just the "high income professionals" against which its provisions are directed and which are singled out in the Taskforce Report…There is no specific targeting of

11 *Submissions 7, 9, 11, 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 34, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47, 48, 49, 50, 51, 52, 53, 55, 57, 75, 76, 89, 90, 91, 92, 93, 94, 115.*

12 *Submissions 7, 9, 11, 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 34, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47, 48, 49, 50, 51, 52, 53, 55, 57, 75, 76, 89, 90, 91, 92, 93, 94, 115.*

13 AFCCRA, *Transcript of Evidence, 6 July 2004,* p.34.

> recalcitrant high income groups that have successfully used and abused the system in the past and hence the Bill's provisions affect widely used methods of separating family and private assets from business related personal liability.[14]
>
> There is nothing in the Bill to prevent its application to middle-income, or even low-income Australians…If the true intention is to restrict the operation of the Bill to "high income professionals" then a statement to that effect should be included in the Bill itself.[15]

## Retrospectivity

3.12 The proposed new Division 4A of Part VI will have retrospective effect.[16] This retrospectivity was the subject of much of the criticism of the proposed change. A recurring theme in submissions was that the proposal was unjust in that it would allow the trustee in bankruptcy to challenge transactions that were legitimate at the time they were entered into:

> ACEA believes that the retrospective nature of the proposed additional powers of the trustee is contrary to reasonable expectations by firms of certainty, particularly when the practice has been viewed as legitimate and is not motivated by fraudulent or dishonest purposes.[17]
>
> The proposed legislation is retrospective in the sense that it potentially alters the future consequences of past events. This effectively leads to a situation where a person undertakes a completely lawful transaction one day and the next has sanctions attached to that action. It is this type of retrospective law about which the most reservations are generally expressed.[18]

3.13 Conversely, some submitters focused on the potential difficulties that trustees in bankruptcy may face as a result of the retrospective nature of the proposed amendments. The IPAA referred to the 'unintended consequences' of this aspect of the proposed change:

---

14 Master Builders Australia, *Submission 58,* p.2.

15 Wesley Community Legal Service, *Submission 87,* p. 1.

16 BLAAAMB 2004, Schedule 1, Item 5.

17 ACEA, *Submission 88,* p.6.

18 Professions Australia, *Submission 81,* p. 28.

> At the time of commencement there could be estates where the Trustee has paid the final dividend to creditors but the estate is still current. Will this Trustee be obliged to now investigate the bankrupt's affairs in relation to the amendments? Will the Trustee be required to fund this investigation him or herself? If the Trustee does not conduct such an investigation, will the Trustee be negligent?
>
> Will the Trustee be required to investigate every current bankruptcy to determine if the amendments apply to that estate? Who will fund the cost of the exercise?[19]

3.14 In a similar vein Howarth Melbourne stated that 'very simply the paper trail is seldom readily available' and that, because the relation back period proposed by the draft Bill exceeds statutory requirements for record keeping, the trustee will be provided with 'unworkable legislation'.[20]

3.15 A further concern raised in relation to the retrospective nature of this proposal was its potential implications for lending practices. The Australian Bankers' Association stated that:

> The concern for the bank, in lending to the small business, is that what it sees in terms of the business's statement of assets and liabilities may be illusory. There may be out there waiting to happen an event which will cause a divestiture of those assets, and that is a very serious concern. Would banks have to inquire into the background of every business that comes along to make an application for finance?[21]

3.16 The potential for the proposed change to impact on lending practices was also raised as an issue by Professions Australia.[22]

## Reverse Onus of Proof

3.17 The Bill provides that, if the trustee alleges that the bankrupt had a 'tainted purpose' in the transfer of property or payment of money, it will be presumed that this is the case. It will then be up to the respondent entity (and the bankrupt if he or she is joined as a party

19 IPAA, *Submission 69,* p.5.

20 Howarth Melbourne, *Submission 74,* p.29.

21 Mr Gilbert, *Transcript of Evidence,* 5 July 2004, p. 82.

22 Professions Australia, *Submission 81,* p.42.

under proposed section 139CA) to rebut this presumption with evidence to the contrary. The Explanatory Memorandum notes the following in relation to this reverse onus of proof:

> This provision must be considered in the context of the proposed new Division 4A. The new Division is intended to address the problem of high income professionals divesting themselves of wealth prior to bankruptcy while continuing to derive a benefit from that wealth. As noted in paragraph 16, while asset protection arrangements are not uncommon, the Government considers that they should not continue to provide protection when an individual becomes bankrupt. Creditors will be denied access to the bankrupt' s real or substantive wealth where a bankrupt has arranged his or her affairs such that very few assets are 'owned'. In presuming that the bankrupt undertook certain transactions prior to bankruptcy with a 'tainted purpose' , the new scheme reflects the Government' s commitment to challenge the legitimacy of asset protection upon bankruptcy.[23]

3.18 A large number of submissions criticised this feature of the proposed changes, claiming that it would place an onerous burden on the respondent entity and the bankrupt. Of particular concern to submitters was the potential difficulty in providing the necessary evidence where the relevant transfer of property had occurred many years previous. Mr Suryan Robert Chandrasegaran noted that, where the property had been transferred a number of decades ago and records of the transfer were not available, it would be 'almost impossible for such an entity to prove its case'.[24] Cleary Hoare Solicitors suggested that the asset owner would have 'extreme difficulty' in locating evidence as to the purpose of a transfer occurring many years before.[25]

3.19 The monetary and emotional cost of rebutting the presumption of a 'tainted purpose' was also raised as an issue by submitters. Cleary Hoare Solicitors stated that 'Even if the asset owner wins, he or she will be put to significant cost and pain over a long period. There are two major costs of litigation: one is dollars and the other is a very

23 BLAAAMB 2004 Explanatory Memorandum, p.11.

24 Mr Suryan Robert Chandrasegaran, *Submission 116,* p. 2.

25 Cleary Hoare Solicitors, *Transcript of Evidence,* 6 July 2004, p.47.

heavy load of negative energy'.[26] AFCCRA noted that 'access to legal resources' in order to rebut the presumption in favour of a 'tainted purpose' may prove difficult for the respondent entity.[27] The Family Law Section of the Law Council of Australia had similar concerns, stating that:

> If the respondent entity is a mother in a family where the principal income earner is insolvent the cost of defending proceedings by the bankruptcy is likely to be catastrophic. The reversal of the onus of proving a tainted intention or purpose will have devastating consequences in the Family Law context.[28]

3.20 A related concern raised was that, in the context of a family breakdown, the non bankrupt spouse or partner may be hindered in his or her efforts to rebut the presumption by a hostile or disinterested bankrupt. The National Network of Women's Legal Services stated that 'the problem is, if the parties have separated, the bankrupt spouse may have no interest in assisting the non-bankrupt spouse to protect their share of the property cake…It would be difficult to obtain the evidence required and an uncooperative former spouse may be able to actively thwart the non-bankrupt's case.'[29] This concern was also raised by the Family Law Section (FLS) of the LCA:

> A recalcitrant bankrupt may not wish to rebut the tainted purpose argument and may in fact make allegations supporting such purpose in order to get even with their spouse or other entity (like a business partner).[30]

## Constitutional Issues

3.21 It was suggested by some submitters that certain features of this proposal may be unconstitutional. These concerns were twofold- that the proposal may not be a law 'with respect to bankruptcy' (refer s51xvii of the Commonwealth Constitution) and that the proposal constituted an acquisition of property not on just terms (refer s51xxxi of the Commonwealth Constitution). Mr Terry Dwyer stated that:

---

26 Cleary Hoare Solicitors, *Transcript of Evidence,* 6 July 2004, p.47.

27 AFCCRA, *Submission 86,* p.2.

28 The FLS of the LCA, *Submission 98,* p. 3.

29 National Network of Women's Legal Services, *Submission 108,* p. 7.

30 The FLS of the LCA, *Submission 98,* p. 4.

> There seems to be some logical difficulty in asserting that a *solvent* person cannot do as he wishes with his money or property. A law founded on the opposite assumption is hardly a law with respect to bankruptcy. It seems rather a law for the unjust acquisition of property- to seize A's property to pay B's debts, for example, seems to be a Constitutionally questionable legislative adventure. [31]

3.22 A further issue raised in this respect was in relation to the reverse onus of proof. Professions Australia suggested that reversing the onus of proof may be unconstitutional as 'A provision such as that creating the Presumption arguably weakens and impairs the supremacy of the law in the administration of justice and constitutes a legislative usurpation of judicial power'.[32]

## Alternatives to Proposed new Division 4A of Part VI

3.23 There were many suggested alternatives to this proposed change. Suggestions included:

- leaving the Act 'as is'- the rationale being that the current claw back provisions in the Act were adequate to achieve the policy objectives of the proposed change;
- strengthening the existing claw back provisions in the Act- namely ss120 and 121; and
- amendments to the Act and / or tax legislation to specifically target individuals who use bankruptcy to avoid paying a tax debt they can otherwise afford to pay.

### No Changes to Current Provisions

3.24 It was the contention of some submitters that the current provisions in the Act are adequate to meet the policy objectives of this proposed amendment- namely, to address the problem of high-income earners using bankruptcy to avoid paying debts that they can afford to pay. McCullough Robertson Lawyers stated that 'The existing provisions in the Bankruptcy Act are largely adequate to meet community

31 Mr Terry Dwyer, *Submission 73,* p.1.

32 Professions Australia, *Submission 81,* p. 36.

needs'.[33] The Queensland Law Society also suggested that the current provisions in the Act were sufficient, stating that the proposal was based on an 'erroneous belief' in relation to the usage of the existing Division 4A of Part VI:

> Such provisions have in fact been used on previous occasions. There may have only been a couple of reported decisions of the courts on section 139D and 139E, but the lack of reported case law does not truly reflect the number of occasions that registered trustees in bankruptcy have referred to these particular provisions of the Act and settled claims based on those sections.[34]

3.25 Other submitters contended that 'the case for change' had not been sufficiently made out. The National Farmer's Federation stated that 'It has not been shown that existing bankruptcy and taxation powers are inadequate to deal with the specific cases raised over deliberate bankruptcy to avoid debts'.[35] The LCA also raised this as an issue.[36]

## Strengthen the Existing Claw Back provisions

3.26 An alternative suggested by a number of submitters was to strengthen the existing claw back provisions in the Act. Section 120 of the Act deals with transfers for less than market value consideration while section 121 deals with transfers to defeat creditors:

> **Section 120 of the Bankruptcy Act**
>
> **(Undervalued transactions )**
>
> *Transfers that are void against trustee*
>
> (1) A transfer of property by a person who later becomes a bankrupt (the *transferor*) to another person (the *transferee*) is void against the trustee in the transferor's bankruptcy if:
>
> (a) the transfer took place in the period beginning 5 years before the commencement of the bankruptcy and ending on the date of the bankruptcy; and
> (b) the transferee gave no consideration for the transfer or gave consideration of less value than the market value of the

33 McCullough Robertson Lawyers, *Submission 61,* p. 3.

34 Queensland Law Society, *Submission 64,* p. 2.

35 National Farmer's Federation, *Submission 109,* p. 1.

36 The IRC of the LCA, *Submission 98,* p. 4.

property.

*Exemptions*

(2) Subsection (1) does not apply to:

(a) a payment of tax payable under a law of the Commonwealth or of a State or Territory; or
(b) a transfer to meet all or part of a liability under a maintenance agreement or a maintenance order; or
(c) a transfer of property under a debt agreement; or
(d) a transfer of property if the transfer is of a kind described in the regulations.

*Transfers that are not void*

(3) Despite subsection (1), a transfer is not void against the trustee if:

(a) the transfer took place more than 2 years before the commencement of the bankruptcy; and
(b) the transferee proves that, at the time of the transfer, the transferor was solvent.

*Refund of consideration*

(4) The trustee must pay to the transferee an amount equal to the value of any consideration that the transferee gave for a transfer that is void against the trustee.

*What is not consideration*

(5) For the purposes of subsections (1) and (4), the following have no value as consideration:

(a) the fact that the transferee is related to the transferor;
(b) if the transferee is the spouse or de facto spouse of the transferor—the transferee making a deed in favour of the transferor;
(c) the transferee's promise to marry, or to become the de facto spouse of, the transferor;
(d) the transferee's love or affection for the transferor.

*Protection of successors in title*

(6) This section does not affect the rights of a person who acquired property from the transferee in good faith and by giving consideration that was at least as valuable as the market value of the property.

*Meaning of transfer of property and market value*

(7) For the purposes of this section:

(a) *transfer of property* includes a payment of money; and
(b) a person who does something that results in another person becoming the owner of property that did not previously exist is taken to have transferred the property to the other person; and
(c) the *market value* of property transferred is its market value at the time of the transfer.

**Section 121 of the Bankruptcy Act**

**(Transfers to defeat creditors )**

*Transfers that are void*

(1) A transfer of property by a person who later becomes a bankrupt (the *transferor*) to another person (the *transferee*) is void against the trustee in the transferor's bankruptcy if:

(a) the property would probably have become part of the transferor's estate or would probably have been available to creditors if the property had not been transferred; and
(b) the transferor's main purpose in making the transfer was:
(i) to prevent the transferred property from becoming divisible among the transferor's creditors; or
(ii) to hinder or delay the process of making property available for division among the transferor's creditors.

*Showing the transferor's main purpose in making a transfer*

(2) The transferor's main purpose in making the transfer is taken to be the purpose described in paragraph (1)(b) if it can reasonably be inferred from all the circumstances that, at the time of the transfer, the transferor was, or was about to become, insolvent.

*Other ways of showing the transferor's main purpose in making a transfer*

(3) Subsection (2) does not limit the ways of establishing the transferor's main purpose in making a transfer.

*Transfer not void if transferee acted in good faith*

(4) Despite subsection (1), a transfer of property is not void

against the trustee if:

(a) the consideration that the transferee gave for the transfer was at least as valuable as the market value of the property; and

(b) the transferee did not know that the transferor's main purpose in making the transfer was the purpose described in paragraph (1)(b); and

(c) the transferee could not reasonably have inferred that, at the time of the transfer, the transferor was, or was about to become, insolvent.

*Refund of consideration*

(5) The trustee must pay to the transferee an amount equal to the value of any consideration that the transferee gave for a transfer that is void against the trustee.

*What is not consideration*

(6) For the purposes of subsections (4) and (5), the following have no value as consideration:

(a) the fact that the transferee is related to the transferor;

(b) if the transferee is the spouse or de facto spouse of the transferor—the transferee making a deed in favour of the transferor;

(c) the transferee's promise to marry, or to become the de facto spouse of, the transferor;

(d) the transferee's love or affection for the transferor.

*Exemption of transfers of property under debt agreements*

(7) This section does not apply to a transfer of property under a debt agreement.

*Protection of successors in title*

(8) This section does not affect the rights of a person who acquired property from the transferee in good faith and for at least the market value of the property.

*Meaning of transfer of property and market value*

(9) For the purposes of this section:

(a) *transfer or property* includes a payment of money; and

(b) a person who does something that results in another person becoming the owner of property that did not

previously exist is taken to have transferred the property to the other person; and

(c) the *market value* of property transferred is its market value at the time of the transfer.

3.27 The comments and suggestions made by the LCA in relation to strengthening these provisions included:

> The principle objection taken by the LCA to Schedule 1 of the BLAAAM is that it seeks to vest third party property in the trustee for the benefit of creditors when the usual connection to bankruptcy (being insolvency and intention to defeat creditors) is not otherwise apparent.
>
> As the Cummins case[37] showed there isn't necessarily anything wrong with the existing bankruptcy laws. The primary issue a trustee will confront is one of proof: how does the trustee prove the bankrupt's intention at a time long past when documents may be long destroyed?
>
> These problems can be acceptably addressed without damaging the integrity of our bankruptcy laws by amending the existing section 120 and 121 to add a number of rebuttable presumptions. In particular:
>
> - Where the debtor fails to lodge a tax return in circumstances where the debtor was obliged to do so and otherwise had a tax liability for that period it can be presumed, for the purpose of section 120 and 121 (subject to the respondent proving otherwise), that the bankrupt was insolvent at (or within a period about) that time.
> - Where the debtor was obliged to do so by law but fails to keep or preserve proper books and records it can be presumed for the purpose of section 120 and 121 (subject to the respondent proving otherwise) that the bankrupt was insolvent at (or within a period about) that time. Such provision would need to reconcile with the bankrupt's obligations to retain books and records (see for example s 270 of the Act).[38]

---

37 *Prentice v Cummins (No 5)* [2002] FCA 1503- the bankrupt had been a QC since 1980, and had not filed a tax return since 1955 (45 years). The ATO was the largest creditor in the bankrupt estate. The trustee commenced proceedings under section 121 of the Act. The court found that a transfer by the bankrupt of his interest in the family home to his wife had been made with the intention to defeat the interests of the ATO as creditor.

38 The IRC of the LCA, *Submission 98,* p.29.

3.28 Pitcher Partners suggested an alternative similar to that proposed by the LCA, stating that, as much of the existing concern related to the practical difficulties associated with the operation of section 121, an option was the create a 'presumption of insolvency' for the purposes of section 121 in circumstances where 'a transfer of property or diversion of income occurred at a time when there was non compliance with various income tax requirements, such as the lodgement of an income tax return, or the payment of an income tax concession'.[39] The IWIRC on the other hand suggested amending section 121 to enhance the trustee's recovery of property powers where 'the bankrupt is either receiving a "benefit" or is in a "position of influence" with respect to the third party and that property'.[40] The optioning of strengthening the current claw back provisions as an alternative to the proposed change was also referred to by a number of witnesses in the public hearings.[41]

## A 'tax problem' Requires Tax-specific Remedies

3.29 A further alternative suggested was to amend the Act and relevant tax legislation to specifically target those who go bankrupt to avoid paying tax debts. Central to this line of reasoning is that, as the Taskforce Report was motivated by the actions of professionals who became bankrupt to avoid paying tax debts that they could afford to pay, any changes should be directly aimed at addressing that particular problem. Moore Stephens HF suggested amending income tax legislation enabling the assessment raised to persons who have received the benefit of the income determined by similar tracing provisions to that proposed but restricted to know taxation liabilities at the time of bankruptcy.[42] The ICAA stated that the operation and fairness of the bankruptcy system should not be changed to facilitate the collection efforts of the ATO and that:

> This should be dealt with by the Income Tax Assessment Act or the ATO adopting more proactive and timely procedures to ensure that high earning fee-for-service professionals are

39 Pitcher Partners, *Submission 102,* p.18.

40 IWIRC, *Submission 80,* p.2.

41 IPAA, *Transcript of Evidence*, 5 July 2004, p.41; AFCCRA, *Transcript of Evidence,* 6 July 2004, p.37; AICD, *Transcript of Evidence,* 6 July 2004, p.67.

42 Moore Stephen HF, *Submission 32,* p.15.

> lodging their tax returns and paying their tax obligations on time.[43]

The ICAA further proposed that, should people fail to discharge their tax obligations and proceed into bankruptcy then:

> …the existing claw back provisions under s139A of the Bankruptcy Act (should) be amended to provide for the period of claw back which currently prevails to be extended by one year for every year that a tax obligation is outstanding. Alternatively, the proposed amendments of the Bill should only apply when it could be clearly demonstrated by the trustee that the acquisition of property acquired by the third party using funds or property provided by the bankrupt was designed to avoid the payment of a tax liability.[44]

3.30 Professions Australia suggested that the objectives of the Bill could be achieved by means such as increasing the resources of the ATO so that it may effectively pursue tax avoiders; increasing the efficiency of ATO debt collection procedures; and increasing the collection and cross referencing of information available to the ATO.[45]

3.31 The NIA similarly suggested that the resources of the ATO should be increased to aid its debt collection activities.[46]

## Other Suggested Alternatives

3.32 CPA Australia suggested that a hierarchy of recoveries was appropriate. This would involve firstly, ensuring that the Income Tax Assessment Act and the Tax Administration Act collection and recovery regimes have been fully pursued, secondly, that the existing mechanisms provided in the Act which make property available for the payment of debts are applied in the first instance and, finally, facilitating resort to the appropriately modified extensive powers envisaged in the draft Bill.[47] The modifications to the draft Bill suggested by CPA Australia included redrafting section 139AFB (dealing with exempt full value transfers of property) to more closely

43 ICAA, *Submission 68,* p.3.

44 ICAA, *Submission 68,* p.3.

45 Professions Australia, *Submission 81,* p.43.

46 NIA, *Submission 114,* p.5.

47 CPA Australia, *Submission 82.1* , p.1.

parallel the scope and operation of current section 123;[48] including a requirement that the trustee must show that the various recovery arrangements currently contained in Part IV Division 3 have been reasonably exhausted in the list of factors for the court to take into account in section 139F of the draft Bill;[49] and developing some flexibility around the concept of non-divisible property in the draft Bill by introducing a discretion to expand on that concept on an individual bankruptcy basis.[50]

3.33 An alternative suggested by Pitcher Partners was to introduce a special act of bankruptcy which would occur where specified taxation obligations, such as the lodgement of an income tax return or the non-payment of tax, is not complied with.[51]

## Other Issues

3.34 An issue arising out of the public hearings was that the proposed change may contain a potential loophole. The provisions allow the trustee to recover money or property from an entity where that money or property has been paid or transferred by the bankrupt. This raises the question of whether it would be relatively easy for an entity to defeat the scheme by effecting a second transfer of the relevant property.

3.35 There is a general anti-avoidance provision in the draft Bill. Section 139AM would allow the trustee to recover property from subsequent transferees where that property had been acquired as part of a 'scheme' designed to defeat the interest's of the bankrupt's creditors. ITSA explained that, in order to satisfy this provision, the trustee would have to demonstrate that a second transfer 'was effectively one transfer and just went through a number of entities'.[52]

3.36 Nonetheless, it was acknowledged by ITSA that the proposed new scheme could 'potentially' be defeated by a second transfer of the property.[53] This was notwithstanding that 'if the person who

48 CPA Australia, *Submission 82.1,* p.3.
49 CPA Australia, *Submission 82.1,* p.1.
50 CPA Australia, *Submission 82.1,* p.13.
51 Pitcher Partners, *Submission 102,* p.17.
52 ITSA, *Transcript of Evidence,* 6 July 2004, p.16.
53 ITSA, *Transcript of Evidence,* 6 July 2004, p.16.

originally received the property was to sell it then the proceeds of the sale of any replacement property could be recovered by the trustee but only from the entity that received the original transfer'.[54]

## The Committee's Concerns

3.37 The Committee's primary concern in relation to this proposal is its potential to impact on arrangements designed to protect assets for the benefit of family members. The retrospective nature of this proposal would allow the trustee to recover property that had been transferred by the bankrupt (or had been acquired with funds provided by the bankrupt) many years prior to the bankruptcy. Where there was no hint or expectation of insolvency, the proposal will deem that these transfers or payments were made with a 'tainted purpose' and the onus to prove otherwise rests with the respondent entity. The proposed change does not require a link between the transfer and the debtor's solvency at the time the transfer was undertaken - this is in contrast to the current claw back provision dealing with transfers to defeat creditors (section 121).[55] It is the Committee's view therefore that the net effect of this proposal is to quarantine creditors from risk and to transfer that risk to the family of the bankrupt.[56]

3.38 Some technical aspects of the proposal are also of concern to the Committee. Section 139F of the draft Bill lists factors that the court has to take into account when determining whether to make an order under the Division. Included in these factors are terms such as 'hardship', 'use' and 'benefit'. These terms are not defined in the draft Bill. In the Committee's view, this lack of clarity would create uncertainty in the application of the proposed provisions.[57]

3.39 There is also the problem of the use of these provisions in the context of a family breakdown. As noted above, a number of submitters raised as an issue that the non bankrupt spouse or partner may be hindered in his or her efforts to rebut the presumption by a hostile or

54 ITSA, *Transcript of Evidence,* 6 July 2004, p.17.

55 Refer section 121(2) of the Act.

56 *Transcript of Evidence,* 6 July 2004, p.39.

57 *Transcript of Evidence,* 5 July 2004, p.27.

disinterested bankrupt. The Committee perceives this a valid concern in relation to the proposal.[58]

3.40 A further concern of the Committee is in relation to the efforts of the ATO to address the problem that motivated this legislative proposal. The Committee is not satisfied that the ATO has put adequate systems in place to ensure that professionals can fail to lodge tax returns for an excessive number of years, and then become bankrupt to avoid that very debt. One of the recommendations of the Taskforce Report was that subsection 16(4) of the Income Tax Assessment Act and section 3C of the Taxation Administration Act be amended to authorise the Commissioner of Taxation to provide publicly available information to prescribed industry or professional organisations. This proposal has not been implemented. It is the Committee's view that such amendments would go some way to addressing the problems identified in the Taskforce Report.

3.41 In any event, the problem of the ATO's failure to ensure the tax compliance of high earning professionals, in one case for 45 years, has largely been overcome. The combination of the GST, ABN and BAS requirements means that such individuals are easily tracked.[59]

3.42 It was the view of the Committee that the weight of evidence supports the Committee's recommendation that the amendments proposed in Schedule 1 of the draft Bill should be abandoned.

3.43 The Committee notes that the current claw back provisions in the Act were used in the *Prentice v Cummins*[60] decision to recover assets transferred by the bankrupt with the intention to defeat the ATO as creditor. However, that decision is the subject of an appeal. An option suggested by a number of submitters, and in particular the LCA, was to strengthen the current claw back provisions in the Act to address the specific problem which motivated these changes- that of high income earners using the bankruptcy system to avoid paying tax debts that they could afford to pay. In the view of the Committee, this would seem preferable to the blanket and exceedingly disproportionate proposed changes.

58 *Transcript of Evidence,* 6 July 2004, pp.6-8.

59 *Transcript of Evidence,* 22 July 2004, p.15.

60 *Prentice v Cummins (No 5)* [2002] FCA 1503.

## Conclusion

3.44 The Committee has concluded that there is no justification established for a legislative amendment which would effectively quarantine creditors from risk and place that risk on to the family of the debtor. Nor has a case been established to render illegitimate transfers that had been undertaken years ago. As noted by a number of submitters, it is entirely reasonable for business people and others to want to divest themselves of certain assets to provide for the future wellbeing of their families should adverse circumstances arise.[61] Moreover, the Committee notes evidence from ITSA that the amendments proposed in Schedule 1 would be unlikely to improve a trustee's ability to recover any additional assets in a Bond or Skase type situation.[62] However, it is also the view of the Committee that there is some case for strengthening the current provisions to specifically deal with the problems identified in the Taskforce Report.

3.45 The Committee also concludes that reforms to tax legislation should be introduced to allow the ATO to provide bankruptcy and related information to professional bodies. This would provide a significant disincentive for professionals to use bankruptcy to avoid their taxation obligations. This information could include information that identifies individuals who have been bankrupt, subject to a Part IX or Part X arrangement under the Bankruptcy Act, or convicted of a tax offence. Such an amendment would reduce costs for professional associations, and would compliment the disciplinary measures that these bodies may undertake.

### Recommendation 2

3.46 **The Committee recommends that:**

- **the amendments contained in Schedule 1 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and other Measures) Bill 2004 be abandoned; and**

61 See for example, *Transcript of Evidence*, 6 July 2004, p.63.

62 ITSA, *Transcript of Evidence*, 22 July 2004, p.8.

- **Insolvency and Trustee Service Australia and the Attorney-General's Department undertake fresh consultation with the Bankruptcy Reform Consultative Forum with a view to strengthening the current clawback provisions in the Act (sections 120 and 121 in particular).**

## Recommendation 3

3.47 **The Committee recommends that subsection 16(4) of the *Income Tax Assessment Act 1936* and section 3C of the *Taxation Administration Act 1953* be amended to:**

- **authorise the Commissioner of Taxation to provide publicly available information to prescribed industry or professional organisations; and**
- **authorise the Commissioner of Taxation to utilise publicly available information for the purposes of the role of Chief Executive of the Australian Tax Office.**

# 4

# Bankruptcy and Family Law Amendments

## Outline of Chapter

4.1 In this chapter of the report the following issues are considered:

- Support for the proposed change.
- Criticism of the proposed change, namely that -
  - ⇒ the proposed change raises jurisdictional issues;
  - ⇒ the proposed change would result in an increased burden on trustees; and
  - ⇒ the combined effect of the Schedule 1 changes (discussed in previous chapter) and these proposals is that couples may be encouraged to separate.
- The Committee's concerns in relation to the proposed change.
- The Committee's conclusion and recommendation.

## Background

4.2 Schedule 2 of the draft Bill proposes changes to both the Act and the *Family Law Act 1975* to clarify the respective rights of the trustee and the non-bankrupt spouse when family law and bankruptcy proceedings exist at the same time.

4.3 The proposed changes will address the following three scenarios:

- Bankruptcy after separation and prior to property being finally dealt with under the *Family Law Act 1975*. The draft Bill contains amendments to provide that:
  - ⇒ if a party becomes bankrupt in the course of family law proceedings, the rights of the trustee will be subrogated to the trustee in bankruptcy;
  - ⇒ the trustee will become a party to the proceedings;
  - ⇒ in any proceedings before the court, the trustee will stand in the shoes of the bankrupt spouse and will have all the rights which the bankrupt would otherwise have in relation to the property proceedings. This will enable the trustee to put submissions in relation to the claims of creditors; and
  - ⇒ the non-bankrupt spouse will have the right to continue the proceedings against the trustee.
- Bankruptcy after separation and subsequent to property being (finally) dealt with under the *Family Law Act 1975*. The draft Bill contains amendments to provide that:
  - ⇒ where orders have been made by the Family Court but not implemented prior to bankruptcy, the doctrine of relation back may continue to apply; and
  - ⇒ the trustee may bring an application to have the proceedings re-heard to take into account the interests of creditors where those interests had not been properly considered.
- Separation after bankruptcy, but prior to property being finally dealt with by the trustee in bankrupt. The draft Bill contains amendments to provide that:
  - ⇒ where a couple separates after one party has become bankrupt but during the period of bankruptcy, the non-bankrupt spouse may seek to have his or her interest in the property recognised and a distribution from the bankrupt estate of any property which has not been dealt with;
  - ⇒ for reasons of certainty, no claim can be made against property that has already been distributed by the trustee; and
  - ⇒ the Family Court would deal with this claim.

4.4 The Attorney-General's Department stated that the interaction between family law and bankruptcy had been a 'vexed issue' since

1975 (the year that the *Family Law Act 1975* was introduced) and described the proposed change in the following way:

> The Bill will effectively merge the Family Court's jurisdiction on bankruptcy and family law matters in cases where these areas interact, and the amendments will allow the Family Court to consider the non-financial contributions of a non-bankrupt spouse for the acquisition of family property.[1]

## Support for the Bankruptcy and Family Law Amendments

4.5 There was some support for this proposal. The FLS of the LCA expressed support for the proposed change but identified conflicting views within the LCA:

> This legislation, at Schedule 2, has probably gone a little bit further than we had expected, so it takes into account all of the considerations under the Family Law Act claim, including needs considerations. So we are not unhappy about Schedule 2, but the insolvency side of the Law Council of Australia is less comfortable with it.[2]

## Criticism of the Bankruptcy and Family Law Amendments

4.6 The following criticisms were raised in relation to this proposal:

- that the proposal raises jurisdictional issues;
- that the proposed change would result in an increased burden on trustees; and
- that the combined effect of the Schedule 1 changes (discussed in previous chapter) and these proposals is that couples may be encouraged to separate.

1 AGD, *Transcript of Evidence*, 6 July 2004, p.11.

2 The FLS of the LCA, *Transcript of Evidence*, 6 July 2004, pp.92-93.

## Jurisdictional Issues

4.7 Some submitters expressed concern that the Family Court would lack the expertise necessary to deal with bankruptcy issues. The proposed change would allow the Family Court to adjudicate on bankruptcy matters in each of the three scenarios outlined above. So, for instance, where a party becomes bankrupt in the course of property proceedings in the Family Court, the Court would have to reconcile the competing claims of the non-bankrupt spouse and the trustee in bankruptcy. The IPAA stated that:

> It is a fact that family law practitioners and judges have very limited experience in the law and practice of bankruptcy. Given the family law's focus on non-financial contributions to a matrimonial arrangement, this will in all likelihood throw up erroneous applications of bankruptcy law. This will, in turn, lead to confusion in the proper application of the Bankruptcy Act.[3]

4.8 The NNWLS suggested that the Family Court be granted exclusive jurisdiction to deal with cases where bankruptcy and family law issues overlap, because:

> … the different approaches to the laws of bankruptcy and family law may mean that women and children are better served by the Family Court which is used to prioritising the needs of dependants.[4]

4.9 The IRC of the LCA suggested that these proposed changes apply also to de facto couples and those in same sex relationships, and that the Federal Court should deal with all these cases:

> As the Family Court is established under the marriages power of the Constitution, that court could not deal with bankruptcy as it applies to the property of the person in de fact or same sex relationships. Logically therefore, if he Government is bent on applying FLA principles to bankruptcy, those provisions should be incorporated into the Bankruptcy Act. It follows that, if a superior court is to be vested with jurisdiction, it is the Federal Court, rather than the Family Court, which should deal with all relationships, as little purpose would be served by allowing the Family Court

3 IPAA, *Submission 69,* p.9.

4 NNWLS, *Submission 108,* p.8.

> to deal with the property of married or formerly-married spouses and the Federal Court to deal with the property of persons in other relationships.[5]

4.10 However, the FLS of the LCA suggested that the appropriate forum would most likely be determined on a case by case basis:

> I am suggesting there would be instances where the Family Court would say , 'The primary issue between the parties here are going to concern the trustee in bankruptcy, and the Family Law Act provisions will be very ancillary to the Federal Court'. In another case it might be that there are all sorts of complicated Family Law Act issues, maybe even collateral children's issues, child support and so on. I imagine the Federal Court might well say, 'This is not for us. We appreciate that there is an insolvency issue there, a bankruptcy issue. Perhaps the Family Court ought to deal with that'.[6]

## Increased Burden on Trustees

4.11 The IPAA identified resource issues in relation to the proposed change:

> We also question who will fund the Trustee to be represented in Family Law Court proceedings, particularly in the circumstance where all of the material assets of the Bankrupt Estate are subject to the Family Law Court proceedings? In this instance, the Trustee is not guaranteed of a successful or partially successful result to enable him or her to pay for his or her representation work in the proceedings, or pay for legal counsel.
>
> Further, Bankruptcy Trustees are not family law experts. Accordingly, where family law proceedings are on foot or being actively contemplated, Trustees will need to obtain expert advice on the family law implication on the Bankrupt estate. This will be an added burden on the Bankruptcy Estate and further, there is no guarantee that the Bankrupt Estate will have sufficient funds at its disposal to obtain such advice.[7]

---

5 The IRC of the LCA, *Submission 98,* pp.33-34.

6 The FLS of the LCA, *Transcript of Evidence,* 6 July 2004, p.94.

7 IPAA, *Submission 69,* p.10.

## Incentive for Couples to Separate

4.12 Some submitters expressed concern that the combined effect of this and the Schedule 1 proposed changes was that couples would be in a better financial position if they separated. Mr Suryan Chandrasegaran suggested that there was a potential problem with allowing the trustee to 'step into the shoes of a bankrupt spouse' in family law property proceedings:

> …the Bill does this without removing the Court's powers to consider the maintenance needs of the non-bankrupt spouse or the interests of the children of the couple. For example, the new section 72(2) will allow the Family Court to order transfer of vested property to the non-bankrupt spouse to fully or partially satisfy any maintenance claim. Proposed section 79(1)(d) allows the Family Court to make orders requiring the relevant bankruptcy trustee to make 'for the benefit of…a child to the marriage', such transfer of property as the court determines.
>
> The Family Court thus has the power to take into account the needs for maintenance of the non-bankrupt spouse and the children of the marriage. These are powers the Federal Court does not have in dealing with a normal bankruptcy application. The Federal Court must only look at the specific factors listed in section 139F(1)…It cannot take into account the hardship which would be suffered by the non-bankrupt spouse or children if property (such as the family home) is sold up.
>
> Under this Bill, a couple and their children would be better off if they separated or divorced when bankruptcy become imminent.[8]

4.13 This 'objectionable outcome' was also raised as an issue by Arnold Bloch Liebler:

> The effect of the Bill could be to force families to contemplate divorce or property settlement to protect their assets or wealth. Schedule 2 of the Bill exempts property the bankrupt is required to transfer under an agreement pursuant to Part VIII of the *Family Law Act* from being divisible property under the Bankruptcy Act (e.g. property settlements,

8 Mr Suryan Chandrasegaran, *Submission 116,* pp.4-5.

> maintenance agreements). A spouse may obtain a more beneficial division of the family assets upon divorce than a court may allow under ordinary Division 4A bankruptcy proceedings where there is no divorce.[9]

4.14 Similar concerns were raised in the public hearings.[10]

## Other Issues

4.15 The FLS of the LCA suggested that there were a number of technical issues with the amendments proposed to the *Family Law Act 1975*.[11]

4.16 The NNWLS suggested that, as the proposed changes will require the bankruptcy trustee to be joined to certain family law proceedings, safeguards must be put in place to protect the privacy of those involved:

> We note that the Bill requires the bankruptcy trustee to be joined as a party in family law proceedings in certain circumstances. However, it must be noted that there are significant issues of privacy, confidentiality and safety which are relevant in the family law but may not be so apparent to persons and agencies operating in the commercial world. Secrecy of address of a wife who has escaped domestic violence, privacy regarding her place of work etc, are of critical importance.[12]

4.17 The IRC of the LCA suggested that any 'legislative carve-out' of the bankrupt's property must fall within the parameters of sub-section 116(2) of the Act (which defines that property of the bankrupt that will not be divisible amongst creditors) and should only take place after general review of what property should be exempt from vesting in the trustee- 'In this way such carve out can be balanced against such other matters as income and superannuation and the interests of creditors generally'.[13] This point was also raised by the IRC of the LCA in the public hearings.[14]

4.18 The NNWLS expressed concern that a spouse may lack adequate access to legal resources to make a claim on the bankrupt's property:

9 Arnold Bloch Liebler, *Submission 97,* p.16.

10 AFCCRA, *Transcript of Evidence, 6* July 2004*,* p.38.

11 See the FLS of the LCA, *Submission 98,* pp.8-9.

12 NNWLS, *Submission 108,* p.9.

13 The IRC, of the LCA, *Submission 98,* p.33.

14 The IRC of the LCA, *Transcript of Evidence,* 6 July 2004, p.76.

> We are also concerned that the trustee will have the resources to run complex legal proceedings but this may be impossible for a spouse- particularly one who has recently been through Family Court proceedings. There is almost no legal aid available for property matters so even the legal fees could take away a home a mother has just secured for her children.[15]

## The Committee's Concerns

4.19 A concern of the Committee is in relation to the jurisdictional aspects of this proposal. For instance, one element of the proposal is that where a couple separates after one party has become bankrupt but during the period of bankruptcy, the non-bankrupt spouse may seek to have his or her interest in the property recognised and a distribution from the bankrupt estate of any property which has not been dealt with. This matter would be heard in the Family Court. However, couples who are not married do not have access to Family Court proceedings. Under these proposals, a non-bankrupt partner in a de facto relationship would not be able to have his or her interest in the property of the bankrupt recognised. In confining its application to circumstances where bankruptcy and family law matters co-exist, the net effect of the Schedule 2 is to exclude whole classes of individuals from these proposed changes.

4.20 The Committee notes the advice given in public hearings that the Commonwealth is seeking a referral of State jurisdiction to enable the Family Law Court to deal with de facto relationships but not same sex couples.

## Conclusion

4.21 The Committee recognises the importance of addressing the problems arising from the interaction between family law and bankruptcy and recommends that these proposed amendments be implemented.

15 NNWLS, *Submission 108,* p.9.

### Recommendation 4

4.22 **The Committee recommends that the amendments proposed in Schedule 2 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 be implemented.**

# 5

# Supervised Account Regime

## Outline of Chapter

5.1 In this chapter of the report the following issues are considered:

- Support for the proposed change.
- Criticism of the proposed change, namely that it:
  - ⇒ could have unintended consequences for bankrupts;
  - ⇒ fails to fully address the trustee's obligations in relation to the operation of the proposed supervised account regime; and
  - ⇒ may impose an additional burden on the bank where the relevant supervised account is held.
- The Committee's conclusion and recommendation.

## Background

5.2 The current income contributions scheme requires bankrupts earning over a threshold to contribute towards their bankruptcy a proportion of their income exceeding the threshold.[1] Generally, the assessed contribution is garnisheed from wages paid to employed bankrupts

---

1 The income contributions scheme is contained in Division 4B of Part VI of the Act. The current threshold is $35 271.60 (after-tax amount) for a contributor without dependants. The threshold increases for each dependant.

or from accounts held by them with a financial institution.[2] There are provisions in the current scheme to allow review and adjustment in circumstances including 'hardship'.[3]

5.3 As noted in Chapter 1, the amendments proposed in Schedule 3 of the draft Bill are intended to overcome the perceived deficiencies in the current income contributions scheme. These proposed deficiencies are made apparent where the bankrupt is not 'employed' or does not operate a bank account in his or her own name.[4] In those circumstances, the existing garnishee powers in the Act may prove ineffective.[5]

5.4 Under the proposed change, the trustee will in certain cases have access to all of the bankrupt's income before it reaches the bankrupt. The trustee will be able to require the bankrupt to pay all of their income into a bank account that is supervised by the trustee.[6] The existing garnishee powers in the Act would then be used by the trustee to draw the assessed contribution from the supervised account.[7] The trustee must not make a determination that the supervised account regime applies to the bankrupt unless the bankrupt has been assessed as liable to pay a contribution and has either not paid the whole of an instalment at the time it became payable, or has not paid the whole of a contribution at the time it became payable.[8]

5.5 The proposed change also provides for agreement to be reached between the trustee and the bankrupt on certain matters. These include the amount and frequency of withdrawals from the account to meet the bankrupt's living expenses (while ensuring that the balance of the account remains sufficient to meet the bankrupt's liability for contributions) and consent by the trustee to additional withdrawals to meet unexpected liabilities or where a balance has accumulated in the

2 The garnishee powers are contained in Subdivision 1 of Division 4B of Part VI of the Act.

3 A bankrupt may apply to the trustee for a determination of a higher income threshold on the basis of 'hardship' (section 139T). A decision of the trustee to make an assessment is reviewable in the first instance by the Inspector-General in Bankruptcy (section 139ZA). An application may be made to the Administrative Appeals Tribunal for review of the relevant decision of the Inspector-General (section 139ZF).

4 BLAAAMB 2004 Explanatory Memorandum, p.5.

5 BLAAAMB 2004 Explanatory Memorandum, p.5.

6 Proposed section 139ZIF, *BLAAAM* 2004.

7 Proposed subsection 139ZIG(8).

8 Proposed subsection 139ZIC(2).

account that exceeds the amount required to meet the bankrupt's contribution amount.[9]

5.6 Decisions made by the bankruptcy trustee will be reviewable in the first instance by the Inspector-General in Bankruptcy,[10] and then by the Administrative Appeals Tribunal.[11]

5.7 The proposed Schedule 3 imposes criminal sanctions for contravention of certain provisions. These offence provisions will apply where the bankrupt breaches requirements including compliance with a 'supervised account notice' (requiring a bankrupt to open a supervised account);[12] provision of certain information to the trustee about the relevant account;[13] and the requirement to make only authorised withdrawals from the account.[14]

## Support for the Proposed Change

5.8 There was some qualified support for the proposed change. The ABA agreed with the proposed supervised account regime provided that its application did not 'place an additional administrative, risk or regulatory burden upon banks that provide a "supervised account" requested by a bankrupt's trustee'.[15] The IRC of the LCA also expressed qualified support for the proposal, stating that:

> In so far as the proposals are only intended to operate where the bankrupt has defaulted in his or her obligations, the LCA lends cautious support to them but recommends the application of the provisions be monitored for any unintended or overtly harsh consequences.[16]

9 Proposed subsection 139ZIG(3).
10 Proposed section 139ZIO.
11 Proposed section 139ZIT.
12 Proposed subsection 139ZIE(6).
13 Proposed subsection 139ZIE(6).
14 Proposed subsection 139ZIG(7).
15 ABA, *Submission 113,* p.5.
16 The IRC of the LCA, *Submission 98,* p.34.

# Criticism of the Proposed Change

5.9 The following criticisms were raised in relation to this proposal:

- that the proposed change could have unintended consequences for bankrupts;
- that the proposed change fails to fully address the trustee's obligations in relation to the proposed supervised account regime; and
- that clarification of certain elements of the proposed change is required to ensure that it does not impact unnecessarily on the bank where the relevant supervised account is held.

## Unintended Consequences

5.10 The IRC of the LCA suggested that the proposed change could result in unintended consequences for bankrupts who do not receive cash funds for the provision of services:[17]

> A bankrupt may choose, rather than working and paying contributions, to cease working and take over the child care responsibilities of the non bankrupt spouse. The bankrupt is liable then to be assessed for the non-financial benefits he receives, but also, potentially, for the work he or she undertakes as primary care giver to the children of the relationship. If the trustee were to make an assessment and require the opening of a relevant account, the receipt of any funds by the bankrupt from the non-bankrupt spouse potentially have to be paid to that account notwithstanding they are for the benefit of the family at large. Given the criminal sanctions attached to any failure to comply with the direction of the trustee to pay money to an account, there is concern as to how these provisions may operate in practice.[18]

17 Note that current section 139Y of the Act provides that the trustee may regard a bankrupt in certain circumstances as receiving reasonable remuneration in respect of employment, work or activities.

18 The ICA of the LCA, *Submission 98*, p.35.

## The Trustee's Obligations under the Proposed Change

5.11 The IPAA expressed concern that the proposed regime failed to provide sufficient certainty in relation to the trustee's obligations. One of these concerns related to the trustee's obligations in relation to tax liabilities:

> The bankrupt may well have structured his or her business activities in a "tax affective manner" but the Trustee may not be comfortable with the legality of these arrangements from a Tax Law perspective. Accordingly, if the Trustee administers the Supervised Account in a less tax effective way than that previously conducted by the bankrupt, could the trustee be personally (and / or the Estate) be held liable for the "extra" payments that will have to be made to the ATO? In these circumstances it would be prudent for a Bankruptcy Trustee to obtain expert tax advice. Who will be liable to pay for this extra impost- the Trustee? the Estate? or through the Estate, the creditors?[19]

5.12 A further concern of the IPAA was in relation to the review process set out in proposed Schedule 3:

> What happens in the circumstance where the bankrupt takes steps to appeal the Trustee's underlying Income Contributions Assessment? If the Income Contributions Assessment is subject to an appeal, will this prevent a Trustee from determining that the Regime will apply to the bankrupt? Section 139ZIC is silent on this issue. It would be preferable if the Trustee could apply the Regime whilst the underlying Income Contribution Assessment is being reviewed under appeal from the bankrupt. Otherwise a bankrupt may use this mechanism to frustrate the Regime.[20]

## Clarification in Relation to ADIs

5.13 The ABA raised concerns in relation to the potential impact of the suggested change on ADIs.[21] In this regard, the ABA submitted that:

---

19 IPAA, *Submission 69,* p.10.

20 IPAA, *Submission 69,* p.10.

21 An 'ADI' is an 'authorised deposit-taking institution'- section 5 of the Act defines this term for the purposes of the Act.

- the proposed legislation should make clear that liability for ensuring that the supervised account is a conforming account should rest with the bankrupt and not the ADI;[22]
- the proposed legislation should exempt the ADI from notice or being put on inquiry as to the existence or otherwise of the trustee's consent for withdrawal from the supervised account by the bankrupt;[23]
- for the avoidance of doubt, the proposed legislation should make clear that an authorised withdrawal is one which is made for a fee or charge imposed by the ADI for the holding and closure of the supervised account;[24] and
- banks should not be put to monitoring or reporting requirements in relation to the supervised account beyond the normal statement of account services that banks customarily provide to their customers.[25]

## Other Issues

5.14 A further concern raised by the IPAA was that, as it failed to provide for an overdraft facility, the proposed supervised account regime would create problems for 'seasonal businesses':

> The Act does not allow for a Trustee to utilise an overdraft facility with respect to the Supervised Accounts Regime. This will pose considerable difficulty in seasonal businesses, particularly where the Regime is commenced during a low cashflow period and where there are extremely good prospects, subject to the bankruptcy being funded in the meantime, of obtaining large cashflow surpluses at a future date. Accordingly, in our opinion, the utilisation of an overdraft account should be left to the discretion of the Trustee.[26]

5.15 The IRC of the LCA suggested that the threshold levels in the current income contributions scheme be reviewed. This submitter referred to

22 ABA, *Submission 113,* p.5- in this regard, the ABA recommended amendments to proposed sections 139ZIE, 139ZIEA, 139ZIF, 139ZIG, 139ZIH, 139ZIHA and 139ZII.

23 ABA, *Submission 113,* p.6.

24 ABA, *Submission 113,* p.6.

25 ABA, *Submission 113,* p.6.

26 IPAA, *Submission 69,* p.10.

'anecdotal evidence' suggesting that even nominal contributions by the bankrupt may cause hardship to families. In the view of the IRC of the LCA therefore, 'considerations should be given to reviewing the threshold levels to ensure that they properly reflect a standard (of) living which will not otherwise cause undue hardship to innocent third parties'.[27]

## Conclusion

5.16 The Committee recognises however that there are potential enforcement problems with the current income contributions scheme and recommends that the proposed amendments be implemented.

### Recommendation 5

5.17 **The Committee recommends that the amendments proposed in Schedule 3 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 be implemented.**

27 The IRC of the LCA, *Submission 98,* p.35.

# 6

# Financial Agreements

## Outline of Chapter

6.1 This chapter of the report addresses the amendments proposed in schedules 4 and 5 of the draft Bill. The amendments in both schedules are concerned with family law financial agreements. The following issues are addressed in relation to the schedule 4 proposed amendments:

- Support for the proposed change.
- Criticism of the proposed change.
- The Committee's concerns.

6.2 The following issues are addressed in relation to the schedule 5 proposed amendments:

- Support for the proposed change.
- Criticism of the proposed change.

6.3 The Committee makes one recommendation encompassing both proposed amendments.

# Proposed Amendment Relating to Claw Back Provisions

## Background

6.4 Schedule 4 of the draft Bill contains proposed amendments in relation to family law financial agreements. As noted in Chapter 2, Schedule 4 proposes to amend the definition of 'maintenance agreement' at subsection 5(1) of the Act to exclude financial agreements entered into under Part VIIIA of the *Family Law Act 1975*. This will allow the trustee to use the Act's clawback provisions (contained in Division 3 of Part VI) to recover property transferred by the bankrupt prior to the commencement of the bankruptcy.[1]

6.5 The Explanatory Memorandum for the draft Bill explained the reasons for this proposed change:

> Division 3 of Part VI includes provisions which allow trustees to recover certain property transferred by the bankrupt prior to the commencement of his or her bankruptcy. These provisions do not apply to transactions arising from the bankrupt's liability under a 'maintenance agreement' or 'maintenance order'. A financial agreement made under Part VIIIA of the Family Law Act is a 'maintenance agreement' for the purposes of the Act.
>
> A financial agreement can be made before or during the marriage or following separation. It is a binding agreement dealing with the distribution of property in the event of the marriage breaking down. It may also provide for the maintenance of either party to the marriage or their children. Financial agreements do not require approval by a court. Nor do they have to be registered with the court. They can only be set aside by the court in circumstances similar to those applying in contract law (such a fraud and undue influence). For these reasons, it is not appropriate that property transferred pursuant to such an agreement is excluded from the property available to pay creditors.[2]

1 BLAAAMB 2004, Explanatory Memorandum, p.36.

2 BLAAAMB 2004, Explanatory Memorandum, p.36

## Support for the Proposed Change

6.6 The FLS of the LCA expressed support for an amendment that would remove financial agreements from the definition of maintenance agreement in the Act, noting that 'They (financial agreements) are undeniably a way of settling property. I am sure the only reason that they were ever there in the definition is that once upon a time there were section 87 maintenance agreements and they were abolished'.[3]

## Criticism of the Proposed Change

6.7 There was no evidence put before the Committee expressing criticism of the proposed change.

# Amendment Providing for a New Act of Bankruptcy

## Background

6.8 Schedule 5 of the draft Bill also deals with family law financial agreements. The amendment proposes to introduce a new act of bankruptcy in proposed paragraph 40(1)(o) of the Act which will occur when a person is rendered insolvent as result of assets being transferred pursuant to a financial agreement under the *Family Law Act 1975*. The effect of this proposed amendment will be that the trustee is able to claim the property transferred under the relevant financial agreement as divisible property in the bankrupt estate. The Explanatory Memorandum for the draft Bill described the proposed amendment:

> The new act of bankruptcy will apply only where the transfer under the financial agreement has the effect of rendering the person insolvent. This would apply only to transfers pursuant to financial agreements and not to other property distributions (for example, property settlements under section 79 of the Family Law Act).
>
> Subsection 115(1) of the Act provides that the bankruptcy of a person shall relate back to, and be deemed to have commenced at, the time of the commission of the earliest act of bankruptcy within a period of six months before the

3 The FLS of the LCA, *Transcript of Evidence*, 6 July 2004, p.91.

> presentation of the petition leading to the person' s bankruptcy. This amendment will allow the trustee to claim the property transferred pursuant to the financial agreement as divisible property in the estate.
>
> Item 2 proposes to insert new subsection 40(7A) which makes it clear that, for the purposes of paragraph 40(1)(o), a transfer of property includes a payment of money and that a person who does something that results in another person becoming the owner of property that did not previously exist is taken to have transferred the property to that other person.[4]

## Support for the Proposed Change

6.9 The IRC of the LCA supported the proposed change, suggesting that such a provision would most likely have the effect of a trustee being appointed earlier than might otherwise be the case.[5] This submitter also expressed concern however that there might be difficulty in establishing the act of bankruptcy.[6]

6.10 The FLS of the LCA also expressed (in broad terms) support for the proposal.[7]

## Criticism of the Proposed Change

6.11 As noted above, the IRC of the LCA suggested that, given there is no requirement in relation to registration of a financial agreement, there may be difficulty in establishing the relevant act of bankruptcy:

> On balance, I prefer to see it (the proposed new act of bankruptcy) there, but the reality is that it is a private agreement between two individuals, unless it is made public…Given that it is a private arrangement, how are you going to prove it?[8]

4 BLAAAMB 2004, Explanatory Memorandum, p.37.
5 The IRC of the LCA, *Submission 98,* p.34.
6 The IRC of the LCA, *Submission 98,* p.34
7 The FLS of the LCA, *Submission 98,* p.1.
8 The IRC of the LCA, *Transcript of Evidence,* 6 July 2004, p.82.

## The Committee's Concerns

6.12 The Committee has some concerns in relation to the amendment proposed in Schedule 4 of the draft Bill. ITSA noted that, by removing financial agreements from the definition of 'maintenance agreement' in the Act, this amendment would 'allow the trustee to recover property transferred at less than market value or as a preferred transfer to a creditor where that transfer occurred pursuant to the terms of the financial agreement.'[9]

6.13 However, it is the Committee's view that such an amendment may have a detrimental impact on those financial agreements involving a transfer of an asset in lieu of maintenance. In that situation, there is a potential for families to be disadvantaged where the trustee is able to recover an asset that has been transferred for the benefit of the family.[10] Moreover, the spouse would be placed in the position of having to appear before the court to defend the trustee's action, which would involve further cost to that party. While ITSA's evidence was that such a situation would not 'necessarily follow',[11] the Committee has reservations in relation to this as a potential outcome.

## Conclusion

6.14 The Committee concludes that the amendments proposed in schedules 4 and 5 should be implemented.

### Recommendation 6

6.15 **The Committee recommends that the amendments proposed in Schedules 4 and 5 of the draft Bankruptcy Legislation Amendment (Anti-Avoidance and Other Measures) Bill 2004 be implemented.**

Hon Bronwyn Bishop MP
Chairman
July 2004

9 ITSA, *Transcript of Evidence,* 6 July 2004, p.4.

10 *Transcript of Evidence,* 6 July 2004, p.4.

11 *Transcript of Evidence,* 6 July 2004, p.4.

A

# Appendix A– List of Submissions

| Submission | Individual/Organisation |
|---|---|
| 1 | Sheahan Lock Partners |
| 2 | Cleary Hoare Solicitors |
| 2.1 | Cleary Hoare Solicitors |
| 2.2 | Cleary Hoare Solicitors |
| 3 | Mr B Backwell |
| 4 | Mr Iain Selkirk |
| 5 | Mr Rob Backwell |
| 5.1 | Mr Rob Backwell |
| 6 | Mr Benjamin Trim |
| 7 | Mr R Smith |
| 8 | Mr Stephen Adrian |
| 9 | Mr Richard Ellis |
| 10 | Mr Alan Boys |
| 11 | Mr Rex Atkins |
| 12 | Mr Kevin Judge |
| 13 | Mr A R M Taylor |
| 14 | Mr Christopher Parkinson |

15 Mr Jeffrey Vibert

16 Mr Ross Williamson

17 Mr Geoff Woods

18 Mr Matt Davis

19 Mr Alan Gerrard

20 Mr James Goodwin

21 Mr Kim Maisey

22 Mr Guy Bailey

23 Mr Mark Leaker

24 Mr Cam Ansell

25 Dr Stephen Emery

26 Mr Simon Corbett

27 Mr Peter Gibbons

28 Mr Malcolm Tew

29 Mr Richard Payne

30 Mr Sean McMahon

31 His Honour John Howse

32 Moore Stephens HF

33 Ronald A Newton & Associates

34 Mr Richard Anderson

35 Mr Lou Di Labio

36 Mr David McKenzie

37 Mr Richard Rowick

38 Mr Simon Line

39 Mr Peter Lock

40 Mr Peter Bacich

| | |
|---|---|
| 41 | Ms Beverley Winterton |
| 42 | Mr Timothy Bailey |
| 43 | Mr Mike Best |
| 44 | Mr John Muntz |
| 45 | Mr Brenton Siviour |
| 46 | Mr Ron Jee |
| 47 | Mr Louis Sauzier |
| 48 | Mr Owen Mitchell |
| 49 | Mr Paul Johnson |
| 50 | Mr Ewen Malcolm |
| 51 | Mr W J Stephen |
| 52 | Mr Peter Folland |
| 53 | Mr Graeme Jolley |
| 54 | Australian Institute of Company Directors |
| 55 | Mr Tony Douglas-Brown |
| 55.1 | Mr Tony Douglas-Brown |
| 56 | Bentleys MRI |
| 57 | Mr Roger Thomson |
| 58 | Master Builders Australia |
| 59 | Moore Stephens BG |
| 60 | Mr Damian Quinn |
| 61 | McCullough Robertson |
| 62 | Australian Industry Group |
| 63 | Mr Donald Campbell-Smith |
| 64 | Queensland Law Society Inc |
| 65 | Law Society of South Australia |
| 66 | Family Law Practitioners Association of Tasmania |

| | |
|---|---|
| 67 | Mr Stephen Hawke |
| 68 | The Institute of Chartered Accountants in Australia |
| 69 | Insolvency Practitioners Association of Australia |
| 70 | Mr John Piper |
| 71 | Name withheld |
| 72 | Name withheld |
| 73 | Dr Terry Dwyer |
| 74 | Horwath Melbourne |
| 75 | Finkelstein Hickmott Pty Ltd |
| 76 | Mr Ian Murie |
| 77 | Australian Medical Association Limited |
| 78 | Sims Partners |
| 79 | Investment & Financial Services Association Ltd |
| 80 | International Women's Insolvency and Reconstruction Committee Australian Network (Qld) Inc |
| 81 | Professions Australia |
| 82 | CPA Australia |
| 82.1 | CPA Australia |
| 83 | National Tax & Accountants' Association Ltd |
| 84 | Society of Trust and Estate Practitioners (STEP) |
| 85 | Speed and Stracey Solicitors |
| 86 | Australian Financial Counselling and Credit Reform |
| 87 | Wesley Community Legal Service |
| 87.1 | Wesley Community Legal Service |
| 88 | Association of Consulting Engineers Australia (ACEA) |
| 89 | Secure Health Management Pty Ltd |

| | |
|---|---|
| 90 | BPA Engineering |
| 91 | B M & Y Chartered Accountants and Business Advisers |
| 92 | Mr Gervase Purich |
| 93 | Security Capital Corporation |
| 94 | Barrymores Pty Ltd |
| 95 | Mr Michael Patterson |
| 96 | Mr David Gold |
| 97 | Arnold Bloch Liebler |
| 98 | Law Council of Australia |
| 98.1 | Law Council of Australia |
| 99 | Australian Venture Capital Association Limited |
| 100 | Law Institute of Victoria |
| 101 | Mr Russell Joseph |
| 102 | Pitcher Partners |
| 102.1 | Pitcher Partners |
| 103 | Buxton Development Projects Pty Ltd |
| 104 | Australian Retailers Association |
| 105 | Ms Fiona Fielding |
| 106 | Mr Robert Kenrick |
| 107 | Mr Simon Aitken |
| 108 | National Network of Women's Legal Services |
| 109 | National Farmers' Federation |
| 110 | Mr George Vumbaca |
| 111 | Victorian Employers' Chamber of Commerce and Industry |
| 112 | The Nationals |
| 113 | Australian Bankers Association |

| | |
|---|---|
| 114 | National Institute of Accountants |
| 115 | Mr Damien Kelly |
| 116 | Mr Suryan Chandrasegaran |
| 117 | Tourism & Leisure Consulting Pty Limited |
| 118 | Financial Planning Association of Australia Limited |
| 119 | Insolvency and Trustee Service Australia |
| 120 | Richard A Bobb Chartered Accountants |
| 121 | Mr Haydn Growden |
| 122 | Mr Andrew Maggs |
| 123 | Mr David Kerr |
| 124 | Mr Russell Stewart |
| 125 | Grantley Bland & Associates |
| 126 | Mr John Volders |
| 127 | Ms Diane Jenner |
| 128 | Mr Geoffrey White |
| 129 | Mr Dennis Robertson |
| 130 | Mr Martin Holgye |
| 131 | Mr Cameron Johnstone |
| 132 | Mr Larry Gilmour |
| 133 | Pitcher Partners NSW Pty Limited |
| 134 | The Law Society of New South Wales |
| 135 | Ferrier Hodgson |
| 136 | Taxation Institute of Australia |
| 137 | Smith Barney Citigroup |
| 138 | Mr John Markos |
| 139 | Mr Cameron Leaver |

| | |
|---|---|
| 140 | Mr Jamie McKeough |
| 141 | Denis & Joan Brion |
| 142 | Ms Helen Yiannikas |
| 143 | Mr Neil Dobbs |
| 144 | Mr Robin Fraser |
| 145 | Mr Tony Protich |
| 146 | Mr Don Munro FCA |
| 147 | Mr Peter Carroll |
| 148 | Mr Mike O'Reilly |
| 149 | Harrisons Insolvency |
| 150 | Mr Allen Wainrit |
| 151 | Mr Richard Jacobs |
| 152 | Mr David Reid |
| 153 | Mr Geoff Brayshaw |
| 154 | Mr Peter Loh |
| 155 | Mr Marc Fabig |
| 156 | Mr Ian Simpson |
| 157 | Mr Richard Knight |
| 158 | Ms Ann Dalton |
| 159 | Mr Anthony Kittel |
| 160 | Mr Matthew Roberts |
| 161 | Mr Jeremy Culver |
| 162 | Ms Marianne Pegoli |
| 163 | McPhee Kelshaw Solicitors & Conveyancers |
| 164 | Baker Taylor Pty Ltd |
| 165 | Mr Richard Brooks |
| 166 | Mr Rubens Locaputo |

| | |
|---|---|
| 167 | Pharmacy Guild of Australia |
| 168 | Mr Alan Peach |
| 169 | Mr John Purcell |
| 170 | Mr Charles Stanford |
| 171 | Grant Thornton, Perth |
| 172 | Mr Stuart Black |
| 173 | Mr R D Leak |
| 174 | Ms Liane Ringham |
| 175 | Mr Michael Perrott |
| 176 | Maddens Lawyers |
| 177 | Australian Taxation Office |

B

# Appendix B – List of Exhibits

| | |
|---|---|
| 1 | Mr John Murphy MP<br>'Various correspondence: Dated between December 2002 and February 2003' |
| 2 | Sheahan Lock Partners<br>'Bankruptcy Judgement from Federal Magistrates Court Adelaide 22 March 2002' |
| 3 | Sheahan Lock Partners<br>'Bankruptcy judgement Federal Court of Australia 25 October 2002' |
| 4 | Mr Lou Di Labio<br>'Press clipping: Weekend Australian 22-23 May 2004' |
| 5 | Mr John Murphy MP<br>'Letter from Attorney-General to Mr John Murphy re Bankruptcy inquiry, dated 22 June 2004' |
| 6 | Confidential |
| 7 | Law Council of Australia<br>'5th ITSA National Congress on 14 May 2004' |

| | | |
|---|---|---|
| 8 | Australian Financial Counselling and Credit Reform Association | |
| | 'Section 139ZQ Notices' | |
| 9 | Master Builders Australia | |
| | 'March 2004 Law Institute Journal, Romauld Andrew "A new framework for the building industry - security of payment and adjudication of progress claims"' | |
| 10 | Insolvency and Trustee Service Australia | |
| | Federal Court and Federal Magistrate Court cases where s120 and 121 of the Bankruptcy Act 1966 have been considered | |
| 11 | NSW Bar Association | |
| | New South Wales Bar Association interaction with ATO regarding bankrupt barristers and avoidance of tax | |
| 12 | The Hon Bronwyn Bishop | |
| | Letter regarding treasures tax return (JCPA Report 326) | |

C

# Appendix C – List of Witnesses

## Monday, 5 July 2004 - Canberra

**Australian Bankers Association**

Mr Ian Gilbert, Director

**Australian Medical Association Limited**

Mr Warwick Hough, Director, Workplace Policy Department

**Australian Taxation Office**

Mr Gregory Farr, Second Commissioner of Taxation

Ms Judith Lind, Assistant Commissioner, Serious Non Compliance

Mrs Megan Yong, Assistant Commissioner, Operations

**CPA Australia**

Ms Judith Hartcher, Business Policy Adviser

Mr John Mann, Chairman of the Board Public Practice Committee

Mr John Purcell, Technical Adviser, Management & Business

**Insolvency Practitioners Association of Australia (IPAA)**

Ms Kim Lee-Anne Arnold, Technical Director

Mr Bruce Carter, President

**Pitcher Partners**

Mr Gess Rambaldi, Partner, Business Recovery and Insolvency Services Division

Mr Andrew Yeo, Partner, Business Recovery and Insolvency Services Division

**Professions Australia**

Ms Beverley Clarke, Executive Director

Miss Linda Johnson, External Consultant, Mallesons Stephen Jaques

**Sims Partners**

Mr Scott Pascoe, Chartered Accountant

**The Institute of Chartered Accountants in Australia**

Mr William Palmer, General Manager Standards and Public Affairs

## Tuesday, 6 July 2004 - Canberra

**Attorney-General's Department**

Mr Kym Duggan, Assistant Secretary

**Australian Attorney-General's Department**

Mr Karl Alderson, Attorney-General's Assistant Secretary, Office of Legal Services Coordination

**Australian Financial Counselling and Credit Reform Association**

Ms Janet Pentland, Chairperson

**Australian Institute of Company Directors**

Mr John Story, Law Committee Member

Ms Gabrielle Upton, Senior Policy Officer

**Cleary Hoare Solicitors**

Mr Michael Hart, Managing Principal

**Insolvency and Trustee Service**

Mr David Bergman, Adviser, Policy and Legislation

**Insolvency and Trustee Service Australia**

Mr Terry Gallagher, Chief Executive and Inspector-General in Bankruptcy

**Law Council of Australia**

Mr Michael Foster, Chairman, Family Law Section

Mr Michael Lhuede, Insolvency and Reconstruction Committee

**Law Institute of Victoria**

Mr Christopher Dale, President

**Law Society of the ACT**

Mr Denis Farrar, President

**Master Builders Australia**

Mr Richard Calver, National Director, Industrial Relations & Legal Counsel

Mr Todd Ritchie, Chief Economist

**Wesley Community Legal Service**

Mr Richard Brading, Principal Solicitor

## Thursday, 22 July 2004 - Sydney

**Arnold Bloch Liebler**

Mr Leon Zwier, Partner

**Attorney-General's Department**

Mr Kym Duggan, Assistant Secretary

**Australian Attorney-General's Department**

Mr Karl Alderson, Attorney-General's Assistant Secretary, Office of Legal Services Coordination

**Australian Taxation Office**

Mr Gregory Farr, Second Commissioner of Taxation

Ms Judith Lind, Assistant Commissioner, Serious Non Compliance

Mrs Megan Yong, Assistant Commissioner, Operations

**Insolvency and Trustee Service**

Mr David Bergman, Adviser, Policy and Legislation

**Insolvency and Trustee Service Australia**

Mr Terry Gallagher, Chief Executive and Inspector-General in Bankruptcy

**NSW Bar Association**

Mr Ian Harrison SC, President

Mr Philip Selth, Executive Officer

D

# Appendix D – List of cases

**Federal Court and Federal Magistrate Court cases where s120 and 121 of the Bankruptcy Act 1966 have been considered**

**Reported on Austlii / Butterworths CaseBase**

**Over period 2000-2004**
**(Created 20 July 2004)**

| Case name | Outcome for trustee on s120/s121 argument |
|---|---|
| Official Trustee in Bankruptcy v Mateo [2003] FCAFC 26 | Unsuccessful |
| Anscor Pty Ltd v Clout (Trustee) [2004] FCAFC 71 | Unsuccessful |
| Clout (Trustee) v Anscor Pty Ltd [2003] FCA 326 (10 April 2003) | Successful |
| Prentice v Cummins (No 5) (includes summary) [2002] FCA 1503 (5 December 2002) | Successful |
| Jabbour v Official Receiver & Ors [2002]FMCA 28 (26 June 2002) | Successful |
| Official Trustee in Bankruptcy v Lopatinsky [2003] FCAFC 109 | Uncertain — remitted to primary judge |
| McVeigh v Long [2002] FMCA 53 (3 May 2002) | Uncertain — only determined trustees standing |

| | |
|---|---|
| Jabbour v Sherwood [2003] FCA 529 (28 May 2003) | Uncertain— matter remitted to magistrate |
| Official Trustee in Bankruptcy v Trevor Newton Small Superannuation Fund Pty Ltd [2001] FCA 1267 | Successful |
| Matthews v Nilant & Ors [2002] FMCA 201 (15 November 20) | Successful |
| Sellers v Tsimiklis & Anor (No.1) [2003]FMCA 139 (11 April 2003) | Successful (on 120) |
| Dare & Anor v Nowbrook Pty Ltd & Anor [2002]FMCA 364 (19 November 2002) | Successful |
| Mateo v Official Trustee in Bankruptcy [2002] FCA 344 | Unsuccessful |
| Worrell & Anor v Pix & Ors [2002]FMCA 93 (6 June 2002) | Successful |
| Official Trustee in Bankruptcy, the Trustee of the Property of Phillip Martin Higgins v Higgins [2000] FCA 1850 | Transferred to Family Court |
| Benson v Cook [2001] FCA 1684 | Unsuccessful |
| Schmierer v Horan & Anor [2004] FMCA 16 (3 February 2004) | Successful on 120 |
| Lumsden v Snelson [2001] FCA 83 | Successful |
| Macks v Morris [2003] FMCA 208 (3 June 2003) | Successful |
| Jones v Southall and Burke Pty Ltd [2003]FMCA 27 (13 February 2003) | Unsuccessful |
| Sellers v One Step Plumbing and Concrete Pty Ltd [2002] FCA 478 | Successful |
| Official Trustee in Bankruptcy v Dunwoody [2004]FMCA 143 (27 February 2004) | Mareva inj sought against possible 121 120, but not granted |
| Permfox Pty Ltd, in the Matter of Chase v Official Receiver for the Bankruptcy District of New South Wales [2002] FCA 1564 | Partially successful on 121 |
| Young v Turner [2003] FMCA 144 (24 April 2003) | Partially successful on 121 |

| | |
|---|---|
| Lopatinsky v Official Trustee in Bankruptcy, in the matter of Lopatinsky [2002] FCA 861 | Unsuccessful on 120 |
| Trustee of the Property of O'Halloran, in the matter of O'Halloran v O'Halloran [2002] FCA 1305 | Successful |
| McBain v Parsons [2000] FCA 935 | Successful |
| Lin v Official Trustee in Bankruptcy (No.1) [2001] FMCA 106 (31 October 2001) | Unsuccessful |
| Pastro v Official Trustee in Bankruptcy [2000] FCA 744 | Successful |
| McVeigh v Zanella [2000] FCA 1890 | Successful |
| Scott v Page [2003]FMCA 439 (7 October 2003) | Successful |
| Lopatinsky v Official Trustee in Bankruptcy, in the matter of Lopatinsky [2003] FCA 1256 | Unsuccessful |
| Prentice v Cummins (No 6) [2003] FCA 1002 | Dealt with another issue |
| Daniel v Daniel, in the matter of Daniel [2004] FCA 648 (18 March 2004) | Unsuccessful |
| Fletcher & Anor v Landgridge & Ors [2002] FMCA 139 (26 July 2002) | Unsuccessful |
| Green v Dare [2003] FCA 172 | Successful |
| Cottrell v Nicholls, in the matter of Cottrell [2003] FCA 1351 | Successful |
| Parsons and Parsons v McBain [2001] FCA 376 (5 April 2001) | Partially successful |
| Jessup (Trustee) v Mountain View Farm [2002] FCA 312 | Unsuccessful |
| Cook v Benson [2003] HCA 36 (19 June 2003) | Successful |
| Zink v Official Receiver [2002] FCA 523 (19 April 2002) | Successful |
| Prentice v Cummins [2002] FCA 1140 | Dealt with another issue |
| Cook v Benson [2003] HCA 36 (19 June 2003) | Successful |

| | |
|---|---|
| Tsimiklis v Sellers [2003] FCA 1257 | Dealt with another issue |
| Prentice v Harrison [2000[ FCA 1764 | Dealt with another issue |
| Cook (Trustee), In the matter of Benson [2000] FCA 1777 | Successful |
| Macks v Morris (No.2) [2003] FMCA 241 (3 July 2003) | Dealt with costs |
| One Step Plumbing & Concrete Pty Ltd v Sellers [2002] FCA 865 | Dealt with other issue |
| Ambrose (Trustee), in the matter of Little (Bankrupt) v Little [2002] FCA 877 (3 July 2002) | Dealt with other issue |
| Cottrell v Nicholls (Trustee) in the matter of Cottrell(Bankrupt) [2004] FCA 358 (25 March 2004) | Dealt with other issue |
| MACKS (as trustee in bankruptcy in the bankrupt estates of HOUSE) v HOUSE— BC200207543 | Unsuccessful |
| Dare & Anor v Nowbrook Pty Ltd & Anor [2002] FMCA 364 (19 November 2002) | Successful |
| Zohar & Ors v Hicks [2002] FMCA 308 (24 December 2002) | Successful |
| Bartrop v Nilant (Trustee), in the matter of Bartrop [2003] FCAFC 306 | Unsuccessful |
| Posnerv Gibb & anor [2001] FMCA 93 (25 September 2001) | Successful |
| Cottrell v Nicholls, in the matter of Cottrell [2003] FCA 1351 | Dealt with another issue |
| Official Trustee in Bankruptcy v Lopatinsky [2003] FCAFC 109 | Unsuccessful |
| Official Trustee in Bankruptcy v Mateo [2003] FCAFC 26 | Unsuccessful |

| | |
|---|---|
| Total number of 2000-2004 cases reported: | 58 |
| No. cases where Trustee successful: | 26 (44.83%) |
| No. cases where Trustee partially successful: | 3 (5.17%) |
| No. cases where Trustee unsuccessful: | 15 (25.96%) |
| No. cases where outcome for Trustee uncertain / decided another issue: | 14 (24.14%) |