Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Additional Estimates

10 – 11 February 2010

Question: aet 71

Topic: Changes in Corporate Law

Hansard Page: Written

Senator EGGLESTON asked:

1. How has the Minister's decision to proceed with changes in corporate law impact on shareholders of companies?
2. Why are shareholders now looking at being relegated to the position of unsecured creditors?
3. On what basis will the business finance costs rise if the legislation does not proceed?
4. Does the Minister accept that shareholders that have purchased shares in a company between a fraudulent act and the company becoming insolvent are not shareholders but rather secured creditors?

Answer:

1. The reversal of Sons of Gwalia will be positive for shareholders as it will assist companies obtain funding for investment and business growth. It will also reduce business costs and aid in business rescue and rehabilitation by increasing the availability of financing options. Where a company is in financial distress, it will reduce the costs and complexity of any reorganisation attempts which will ultimately benefit shareholders and creditors.
2. The widely understood position prior to the Sons of Gwalia decision was that any claim by shareholders of an insolvent company would rank below claims by other creditors. The High Court in Sons of Gwalia found that shareholder compensation claims would rank with unsecured creditors. To eliminate any uncertainty created by this decision, the Government has announced that it will introduce legislation to ensure that the law largely reflects the position that was widely understood prior to the Sons of Gwalia decision. This will provide greater certainty for shareholders, businesses and providers of finance.
3. Stakeholders have expressed a number of concerns regarding the potential for business financing costs to increase if the legislation does not proceed. The capacity of Australian companies to raise debt finance has been reduced due to concerns about the risk of shareholder class actions. I am aware that finance providers have priced in the risk of a Sons of Gwalia like action, when determining the terms on which finance will be provided. The decision in Sons of Gwalia has the effect of decreasing the returns to credit providers, including finance companies and other businesses providing goods and services to the

company on credit, in the event of insolvency. Creditors have increased the costs of credit, restricted the supply of credit and supplied credit on more onerous terms. This increases business costs and reduces the ability of the company to invest to create shareholder wealth. This leads to an overall negative impact on shareholders greater than any benefit in favour of aggrieved shareholders. The reversal will ensure that such risk will no longer form part of the risk factors for finance providers when determining whether to loan money to Australian companies.

4. Shareholders of insolvent companies who have been misled should seek independent legal advice regarding the legal avenues open to them to receive compensation for their loss. The order of priority of shareholders in the distribution from the proceeds of an insolvent company is determined by the provisions of the *Corporations Act 2001*.