



Insolvency Practitioners
Association of Australia

13 February 2007

**The Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Suite SG.64
Parliament House
Canberra ACT 2600**

Dear Mr Sullivan,

**Inquiry into the Exposure Draft of the Corporations Amendment
(Insolvency) Bill 2007 and related draft regulations**

We refer to your letter of 14 December 2006 in which you invited the IPAA to make a written submission to the above inquiry. The IPAA appreciates the opportunity to make this submission.

Notwithstanding that the Corporations Amendment (Insolvency) Bill 2007 and related draft regulations ("the Bill") does not incorporate all of the recommendations that were outstanding in respect of Corporate Insolvency, it is an excellent package providing much needed reforms. The IPAA and the insolvency industry generally are closely anticipating the commencement of the Bill.

Whilst we recognise that there are some matters that the IPAA would have liked to have seen included in the Bill, for example Recommendation 55, there are no matters of such significance that the commencement of the Bill should be delayed.

Considering specifically the recommendations of the Parliamentary Joint Committee on Corporations and Financial Services' ("the Committee") report "Corporate Insolvency Laws: a Stocktake" ("the Report") highlighted in your letter, the IPAA makes the following comments:

The regulation of the Insolvency Process

Recommendation 7

The Committee recommends that the Government consider establishing an advisory council comprising representatives of professional organisations including the Insolvency Practitioners Association of Australia, CPA Australia, the Institute of Chartered Accountants in Australia, and the Law Council to assist ASIC in relation to the regulation, appointment, registration and removal of registered and official liquidators as well as on issues relating to the maintenance of professional standards of insolvency practitioners.

The IPAA has no objection to this recommendation and would be agreeable to appointing a representative to participate in such an advisory council if one is established. However, we do not see that this would be a recommendation that needs to be legislated for.

Recommendation 8

The Committee recommends that, in its enforcement programs for the lodgement of reports as to the affairs of a company (RATAs), ASIC take greater account of the quality of reports provided.

The IPAA has no objection to this recommendation. However, we do not see that this is a recommendation that needs to be legislated for.

Recommendation 13

The Committee recommends that insolvency be removed as a prerequisite for the avoidance of uncommercial transactions which may be challenged by a liquidator. Such transactions are to have taken place during the two year period preceding formal insolvency.

The IPAA sees merit in this proposal which will bring the relevant Corporations Law provisions into line with the equivalent regime under the Bankruptcy Act, but suggests that care be taken in the drafting of any amendment, so that there is consistency in its application, with Part 2D.1 of Chapter D, noting that as regards the duties imposed on directors and other officers under section 180(1), directors are entitled to rely on the so called business judgment rule. A fine line needs to be drawn between giving Liquidators the necessary powers to set aside transactions which are intended to defeat creditors' interests, and enabling directors to implement a legitimate corporate reorganisation, which is in the interests of the company, its creditors and employees.

The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 33

The Committee recommends that the Government consider the proposal to create a statutory process analogous to a Mareva injunction to enable the courts to freeze assets of a director or manager which are prima facie assets on which the corporation has a just claim.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 35

The Committee recommends that ASIC consider establishing a hot-line and guidelines for its operation in conjunction with strategically located employees for the purpose of facilitating possible early detection of, and intervention to prevent the implementation of, illicit phoenix activities.

The IPAA has no objection to this recommendation and believes that the establishment of the Assetless Administration Fund that is administered by ASIC will assist with the management of illicit phoenix activities by funding liquidators to investigate those companies with no assets.

Recommendation 37

The Committee recommends that in its enforcement programs for the lodgement of external administrators' statutory reports, ASIC also take greater account of the quality of reports provided.

The IPAA has no objection to this recommendation; however, it is important that ASIC also have regard to the quality of financial information that is available to the external administrators when they are preparing their reports. The information in a report is not necessarily a reflection of the quality of the report, but rather the quality of the financial information. In our opinion, the implementation of this recommendation should be directly related to recommendations 8, 9 and 10.

We do not see that this is a recommendation that needs to be legislated for.

Recommendation 47

The Committee recommends that the Government clarify the priority afforded superannuation contributions required to be made after the relevant date of an external administration.

Item 7 clarifies the position where the relevant date falls after, during and at the commencement of a SGC quarter and there is a continuing superannuation obligation after the relevant date.

However, since consultation with Treasury during the IPAA's participation on the Insolvency Law Advisory Group, it has been brought to our attention that there is a potential issue in respect of the external administrator's liability for superannuation contributions on dividends paid to employees for pre-appointment wages. It is the ATO's opinion that where an external administrator makes a dividend in relation to pre-appointment employee entitlements and the external administrator does not make a superannuation contribution in respect of that dividend, a liability for Superannuation Guarantee Charge will arise. This SGC debt will be a debt of the external administrator – in a liquidation entitled to a priority under section 556(1)(dd) (Note: This may change to a priority under section 556(1)(a) once the Bill is passed due to the operation of proposed section 556(1B), (1C) and (1D)).

In the IPAA's opinion this position is untenable for the following reasons:

- A superannuation obligation arising as a result of the payment of a dividend should not be a debt of the administration. Superannuation obligations on pre-appointment entitlements should themselves be a pre-appointment debt, payable in accordance with the priorities under section 556.
- An external administrator may not have an obligation to pay superannuation on these entitlements (the external administrator's obligation would be dependent on the terms of the relevant award or contract of employment), yet failure to remit superannuation will result in a SGC debt.
- If a liquidator is provided with funds under section 560 to meet employee entitlements, he/she may not have sufficient funds available to meet any SGC debt. For example at the moment payments by DEWR under the GEERS scheme does not include superannuation.

- It is considered highly likely that when advising the ATO of the pre-appointment liability for SGC, outstanding pre-appointment wages are being included to determine the amount outstanding. This means that the ATO may be claiming twice for SGC on pre-appointment entitlements.
- Pre-appointment obligations should be provable as a claim in the external administrator, not as a debt of the external administration.

The IPAA recommends that the Corporations Act be amended to clarify that any SGC or superannuation obligations relating to pre-appointment entitlements is a pre-appointment debt that is provable in the administration.

This issue has been raised with Treasury in our submission on the Bill.

Recommendation 52

The Committee recommends that the law be amended to clarify that a DCA which incorporates any form of promise of future performance should not be regarded as finalised until all such promises have been fulfilled.

The IPAA suggests that the problem that the Committee seeks to address via recommendation 52 is more as a result of a lack of understanding of the result of a Deed of Company Arrangement (“DOCA”) rather than a deficiency in the Corporations Act. Implementation of recommendations 50, 51 and 53 will ensure creditors have a better understanding of their rights in respect of DOCAs. The cornerstone of DOCAs is their flexibility. If creditors are fully informed, they should have the right to accept whatever DOCA they want. The IPAA would be slow to support any proposal which fetters the flexibility of the current system, or dictates what a DOCA should or should not contain, subject to the general matters to be set out in it as specified in section 444A(4).

Furthermore, in May 2005 ASIC released a comprehensive guide in respect of Creditor Trust Deeds, the principle means by which Deeds are structured to allow for completion of the DOCA where future performance is still required. This document sets various guidelines to ensure appropriate application of Creditors’ Trust Deeds and that creditors are fully informed.

Recommendation 54

The Committee recommends that the creditors’ voluntary liquidation procedure should be retained and entry to the procedure simplified to enable directors to place a company immediately into liquidation. Where an enterprise is not viable, the law should allow for its swift and efficient liquidation to maximise recoveries for the benefit of creditors.

We note that items 89 to 91 provide for an improvement to the process for the commencement of Creditors’ Voluntary Liquidations. With a lengthening of the period in which to hold the first meeting of creditors, it means that by using the consent to short notice provisions, a meeting of members can be convened immediately after the director’s meeting to appoint a liquidator.

Although this is a significant improvement over the existing process, the IPAA preferred position is that director’s be able to appoint a liquidator by resolution at a

meeting of directors, as is currently the means by which directors appoint a Voluntary Administrator.

The IPAA notes that there is a need for further amendments to section 497 to properly provide for the liquidator to conduct the first meeting of creditors and these matters have been raised with Treasury in our submission on the Bill.

The role of Administrators

Recommendation 3

The Committee recommends that an administrator should be prohibited from using a casting vote in a resolution concerning his or her replacement.

The IPAA is supportive of this recommendation as it was a view put forward by the IPAA in its submissions. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 12

The Committee recommends that reg. 5.3A.02 - administrator to specify voidable transactions in statement - be amended to include rights of recovery against the company's directors for insolvent trading.

The IPAA is supportive of this recommendation. The IPAA's Statement of Best Practice on the Content of Administrator's Reports requires our members to provide information to creditors about possible insolvent trading. An excerpt from clause 7.4 of the Statement of Best Practice states:

"The administrator's report shall include comment regarding whether the company engaged in insolvent trading and may provide an estimate of the loss incurred by the company as a result."

However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 18

The Committee further recommends that ASIC publish a guidance note to assist administrators in ensuring that administrators include all matters material to the creditors' decision in their administrator's report.

The IPAA already provides such a guidance note to its members. The IPAA's Statement of Best Practice on the Content of Administrator's Reports requires our members to include all matters material to the creditors' decisions in their administrator's report and provides guidance on what type of information should be provided.

The recent decision of the Federal Court in the matter *Dean-Willcocks v CALDB*¹ illustrates the importance of compliance with professional standards.

¹ 2006 [FCA] 555

Recommendation 24

The Committee recommends that ASIC work with the professional bodies to encourage the promotion of best practice standards in remuneration charging and in particular the provision of adequate disclosure of the basis of fees charged by insolvency practitioners and on a more timely basis.

It is our understanding that ASIC are currently working on the development of a remuneration guide which would meet this recommendation. The IPAA is also working to update its Statement of Best Practice – Remuneration.

Recommendation 25

The Committee recommends that an administrator should be prohibited from using a casting vote in a resolution concerning his or her remuneration.

The IPAA is supportive of this recommendation as it was a view put forward by the IPAA in its submissions. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 55

The Committee recommends that the law be amended so as to permit administrators to apply to a court for an order that a party to a contract may not terminate the contract by virtue of entry by a company into voluntary administration. The court should be satisfied that the contracting party's interests will be adequately protected.

Although this recommendation is not completely in line with the view put forward by the IPAA in its submissions, the IPAA is supportive of the recommendation. We note that the Government rejected this recommendation in its response to the report. In our submission to Treasury on the Bill, the IPAA has included this matter as one which will remain on our reform agenda. However, the IPAA would not want this issue to delay the commencement of the Bill.

The Role of Directors

Recommendation 10

The Committee recommends that the Government consider amending the law to permit an administrator or a liquidator to recover from directors who have failed to ensure that company records are complete and up-to-date, the costs and expense of reconstructing the company's financial records in order to prepare a full and complete report on the affairs of the company. Directors would be held jointly and severally liable.

The IPAA supports this recommendation. We believe that implementation of this recommendation, along with recommendations 8 and 9, would assist liquidators with their investigations of failed companies and the identification of phoenix activities. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 14

The Committee recommends that the threshold test permitting directors to make the initial appointment of an administrator under the voluntary administration procedure be revised in order to alleviate perceptions that the VA procedure is only available to insolvent companies. The Committee notes the suggestion that the test be reworded to read 'the company is insolvent or may become insolvent'.

The IPAA has no objection to this recommendation. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 31

The Committee recommends that ss 206D and 206F should not be subject to a requirement to have managed two or more failed corporations. They should permit a court, or ASIC in its discretion, to disqualify a person from being a director where essentially two conditions are met: the person is or has been a director of a company which has failed (as defined in s 206D(2)) and the person, as a director of the company (either taken alone or taken together with his/her conduct as a director of any other company) makes him or her unfit to be concerned in the management of a company.

The IPAA has no objection to this recommendation. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 54

The Committee recommends that the creditors' voluntary liquidation procedure should be retained and entry to the procedure simplified to enable directors to place a company immediately into liquidation. Where an enterprise is not viable, the law should allow for its swift and efficient liquidation to maximise recoveries for the benefit of creditors.

Refer to our comments above under the heading "The regulation of the Insolvency Process".

The rights of creditors including the treatment of employee entitlements

Recommendation 43

The Committee recommends that the Minister for Finance request the Corporations and Markets Advisory Committee to review the operation of the Corporations Law Amendment (Employee Entitlements) Act 2000 to determine its effectiveness in deterring companies from avoiding their obligations to employees. Furthermore, in light of the evidence suggesting that some corporations deliberately structure their business to avoid paying their full entitlements to employees and more generally unsecured creditors, the Committee recommends that the review look beyond the effectiveness of the Act and consider, and offer advice on, possible reforms that would deter this type of behaviour.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 44

The Committee recommends that the Government explore the various measures proposed for safeguarding employee entitlements such as insurance schemes or trust funds giving particular attention to the costs and benefits involved in the schemes.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 47

The Committee recommends that the Government clarify the priority afforded superannuation contributions required to be made after the relevant date of an external administration.

Refer to our comments above under the heading “The Regulation of the Insolvency Process”.

The need for empirical research and review processes

Recommendation 29

The Committee recommends that, as a step towards a better understanding of the nature, effects and extent of insolvent assetless companies, the Government should commission an empirical study of assetless companies.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 30

The Committee further recommends that as a first and immediate step, ASIC begin to collate statistics on insolvent assetless companies and publish such figures on a triennial basis together with an analysis.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 32

The Committee recommends that the Government in association with the Council of Australian Governments review the adequacy of the arrangements for the checking of the business names of companies on State Business Names Registries against the ASCOT database of company names and ACNs.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 34

The Committee recommends that the Government review the processes in place for registering a company with a view to improving the measures for determining the bona fides of those applying to register a company.

The IPAA supports this recommendation. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 40

The Committee recommends that ASIC consider enhancing its capacity to provide more comprehensive, comparable analyses of statutory reports of liquidators for the assistance of journalists, academic researchers, the public and the Government and its own management requirements. Such information should be assessed in terms of maintaining public confidence in the administration and enforcement of corporate laws.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 41

The Committee recommends that ASIC continuously evaluate the incidence of possible failures to keep books and records adequately as disclosed in external administrators reports on an annual comparative basis. This measure would allow ASIC to assess the effectiveness of its annual programs for the enforcement of financial reporting requirements.

The IPAA supports this recommendation. However, the IPAA would not want this issue to delay the commencement of the Bill.

Recommendation 43

The Committee recommends that the Minister for Finance request the Corporations and Markets Advisory Committee to review the operation of the Corporations Law Amendment (Employee Entitlements) Act 2000 to determine its effectiveness in deterring companies from avoiding their obligations to employees. Furthermore, in light of the evidence suggesting that some corporations deliberately structure their business to avoid paying their full entitlements to employees and more generally unsecured creditors, the Committee recommends that the review look beyond the effectiveness of the Act and consider, and offer advice on, possible reforms that would deter this type of behaviour.

Refer to our comments above under the heading "The rights of Creditors, including the treatment of Employee Entitlements".

Recommendation 58

The Committee recommends that the Government support a program of research into the impact of insolvency procedures, if necessary, by providing a specific allocation for the conduct of such research by ASIC, the professional associations and/or commissioned researchers.

The IPAA has no objection to this recommendation. The IPAA would not want this issue to delay the commencement of the Bill.

The IPAA appreciates the opportunity to make a submission and we would be pleased to answer any questions or provide any further information the committee may require. We note that the committee will be meeting on the morning of Monday the 5th March in Melbourne. I confirm that we will attend.

Yours sincerely

A handwritten signature in black ink, appearing to read 'J Melluish', written in a cursive style.

J Melluish
President