Submission

Exposure Draft

Corporations Amendment (Insolvency) Bill 2007

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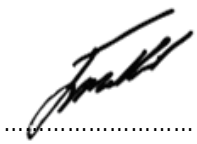

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John Melluish
President

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1. Introduction

The IPAA is the peak body for the Insolvency Profession.

We have worked closely with the Government in the development of the package and commend the government for the extensive consultation process, both in the initial development and the current consultation prior to the submission of the bill to parliament.

This document represents the consolidated views of the Insolvency Profession. The IPAA has conducted an extensive consultation process with its members which included:

- The preparation of detailed briefing papers and articles
- The holding of explanatory briefings around Australia
- The holding of workshops in five capital cities to gain direct feedback
- The conduct of an on-line survey
- The receipt of written feedback

Not all members agree on all issues and those with strong views were encouraged to provide feedback directly to Treasury.

The document is structured to facilitate the understanding of the IPAA position. Each section contains:

- an exposition of the principle involved,
- the rationale why we believe that an amendment is warranted and
- pointers to where the bill may need redrafting

There are a number of issues not addressed in the reform package that the IPAA believes are important for the efficient and effective operation of the insolvency Regime in Australia. These issues are set out in Sections 20 and 21. We strongly urge that the issues identified in section 20 be included in the current reform Bill.

Items in Section 21 are important, but we recognise that they are significant matters and we would not want to delay the Bill to wait for these to be included. We do however wish to continue consultation on these matters with Treasury.

2. Administrator to make available a Statement of Independence (ES pg33)

2.1 Principles

2.1.1 The requirement to disclose relationships that the practitioner is likely to have should be removed

Rationale

It is unreasonable to require practitioners to be able to identify and disclose potential future relationships in the Declaration of Relevant Relationships. There is a requirement for the administrator to update the declaration should the declaration become out-of-date or the administrator becomes aware of an error. This requirement should be sufficient to ensure that as relationships arise, they are declared.

Amendments required

Refer to the comments below in 2.1.3 Amendments required.

2.1.2 Administrators should not be required to disclose relationships of a trivial nature

Rationale

There is significant concern amongst the profession about the level of disclosure that is going to be required to satisfy the requirements of the Declaration of Relevant Relationships. We recognise that the Explanatory Statement suggests a two page limit, however, we also understand the mindset of insolvency practitioners who are concerned to ensure that they do the right thing and disclose every relationship.

The IPAA do not wish to see a situation whereby creditors are overwhelmed with information, most of which is meaningless. The IPAA suggests that trivial relationships be excluded from the Declaration of Relevant Relationships.

"Trivial" is defined in the Macquarie Dictionary as "of little importance, trifling, insignificant". It would be up to the administrator to determine whether a relationship is trivial. The IPAA is prepared to provide guidance in its revised Statements of Best Practice on the issue of trivial relationships.

Failure to disclose a relationship which is not trivial would be an offence and the proposed reasonableness defence could also be applicable to relationships which are not disclosed due to the administrator deeming them as trivial.

Amendment required

The IPAA suggests that either:

- a further clause be added to the definition of declaration of relevant relationship in section 9 excluding the need to disclose trivial relationships; or
- relevant relationship is defined in section 9 to exclude trivial relationships.

2.1.3 There should be a time limit set for the Declaration of Relationships

Rationale

There is significant concern in the profession about the lack of time limit on the declaration of relationships. We recognise the government's concern to ensure that creditors receive complete information with which to make a decision. However, the IPAA suggests that the imposition of an appropriate time limit would not adversely affect creditors, yet would provide a greater level of certainty to insolvency practitioners. We suggest that two years would be appropriate.

Our basis for selecting two years as the appropriate timeframe is as a result of the "Continuing Professional Relationship" requirements in The Institute of Chartered Accountants' APS7 and the IPAA's Code of Conduct ("CPC"). The requirement in APS7 and the CPC is that:

(a) Except in the case of a members' voluntary winding up:

i. No person in a practice shall accept appointment as liquidator, provisional liquidator, controller, scheme manager, or administrator of a company if any person in the practice has, or **during the previous two years** has had, a continuing professional relationship with the company.

ii. No practice or person in a practice shall accept appointment as auditor of a company if any person in the practice has been a liquidator, provisional liquidator, controller, scheme manager, official manager or administrator **within the previous two years**. (emphasis added)

(b) For the purpose of (a)(i) above, a "continuing professional relationship" shall not arise:-

i. by reason only of the appointment or engagement of a practice or person in a practice to investigate, monitor or advise on the affairs of a company on behalf of a third party, so long as the professional obligation is to a party other than the company being investigated, or

ii. if the professional relationship existed for less than two months, or

iii. by reason only of the appointment of a person as provisional liquidator of a company in which the person or any other person in the practice has been administrator, or

iv. by reason only of the appointment of a person as liquidator of a company in which that person or any other person in the practice has been liquidator, provisional liquidator, or administrator, or

v. by reason only of the appointment of a person as controller of a company in which that person or any other person in the practice has been controller under a prior ranking debenture or where the appointment has been made by the Court, or

vi. by reason only of the appointment of a person as scheme manager or administrator of a company in which that person or any other person in the practice has been official manager, liquidator, controller, provisional liquidator or administrator.

Amendments required

The IPAA suggest the following amendment (which incorporates the time limit and the removal of the requirement to disclose possible future relationships):

(a) stating whether any of the following:

(i) the administrator;

(ii) if the administrator's firm (if any) is a partnership—a partner in that partnership;

(iii) if the administrator's firm (if any) is a body corporate—that body corporate;

has had *in the previous two years or currently has* ~~or is likely to have~~ a relationship with:

(iv) the company; or

(v) an associate of the company; or

(vi) a former liquidator, or former provisional liquidator, of the company; or

(vii) a person who is entitled to enforce a charge on the whole, or substantially the whole, of the company's property; and

(b) if so, stating the administrator's reasons for believing that none of the relevant relationships result in the administrator having a conflict of interest or duty.

2.1.4 Insolvency Practitioners that are nominated to replace incumbent administrators should be required to table Declarations of Indemnities and Declarations of Relationships prior to a resolution being put to the meeting.

Rationale

In order that creditors can make an informed decision about whether to replace an incumbent administrator with one nominated to replace the incumbent, creditors should be provided with Declarations of Indemnities and Relevant Relationships by the nominated replacement administrator. Failure to provide creditors with this information will result in creditors having to make a decision about replacing the incumbent administrator with no information on hand to consider the suitability or otherwise of the nominated replacement.

There are concerns among the insolvency profession that the information provided in the Declaration of Relevant Relationships may give a perception of a lack on independence even where the practitioner is independent (for example, in a small community, the practitioner and the directors may be members of the same club, yet they may not actually know each other). Requiring a proposed replacement administrator to provide a Declarations of Relationships may help mitigate this problem as both the incumbent and proposed replacement administrators will have had to provide the same information to creditors and will be treated on an equal footing. It may well be that the proposed replacement administrator's relationships are of more concern to the general body of creditors than the incumbent.

Amendments required

At the moment there is only a requirement for a replacement administrator under s 449C(4)(b) to provide a declaration.

A practitioner that is nominated to replace an incumbent administrator under section 436E(4) should be required to table Declarations of Indemnities and Relevant Relationships prior to the resolution being put to the meeting.

A practitioner that is nominated to act as the administrator of a DOCA (if different to the administrator of the Voluntary Administration) should be required to table Declarations of Indemnities and Relevant Relationships prior to the resolution that would result in his/her appointment being put to the meeting (s 444A(2)).

A practitioner that is nominated to act as liquidator (if different to the Voluntary Administrator) should be required to table Declarations of Indemnities and Relevant Relationships prior to the resolution that would result in his/her appointment being put to the meeting. (s 446A(4))

2.1.5 Liquidators appointed by Members in Creditors Voluntary Liquidations should be required to provide Declarations of Indemnities and Declarations of Relationships.

Rationale

With the amendments to the commencement of Creditors' Voluntary Liquidations ("CVL"), it is envisaged that there will be a lot more companies entering directly into CVL rather than via a Voluntary Administration. As such, the IPAA believes that the requirements for a Declaration of Relevant Relationships and Declaration of Indemnities should be extended to include Liquidators of CVLs. The declarations should be provided with the notice of meeting sent to creditors and tabled at the first meeting of creditors.

Amendment required

A provision similar to proposed 436DA should be inserted for Liquidators of CVLs where the appointment is made by the members.

2.2 Drafting

2.2.1 We suggest that the heading in the Explanatory Statement for this section be changed from "Administrators to make available a statement of independence" to "Declarations by administrator – indemnities and relevant relationships" to more properly represent the declarations that are being made.

2.3 Unresolved Questions

2.3.1 In the Declaration of relevant relationships, if the administrator's firm is a body corporate, do the directors of that body corporate have to declare relationships?

2.3.2 Is it envisaged that a practitioner will have to disclose if they have a personal banking relationship (ie mortgage) with a bank that is entitled to enforce a charge on the whole, or substantially the whole, of the company's property?

3. Factors for consideration by a court in setting remuneration (ES p35)

3.1 Principles

3.1.1 The factors set for consideration by the Court may become factors applicable to creditor fee approval.

Rationale

There is concern amongst the profession that this will happen in two ways:

1. If a application is made to Court, the Court will want to know the creditor's attitude towards the level of remuneration sought and what information was given to creditors when seeking approval of remuneration. The Court may expect that creditors would have been provided with information to enable them to consider the same factors as the Court considers.
2. Guidelines on remuneration may develop which incorporate the Court factors as matters which must be addressed with creditors.

Amendment required

The IPAA suggests that there needs to be additional information added to the Bill and the Explanatory Statement clarifying that the factors for consideration by the Court are applicable only to Court applications for fee approvals.

3.1.2 Market rates of remuneration may not be an appropriate matter to include in the list of court factors.

Rationale

There has been a lot of concern expressed by practitioners about how they will be able to provide information about market rates to assist the Court when the Court is considering their application. The IPAA agrees that being able to provide this information for the Court may be difficult.

Furthermore, what are "market rates"? An insolvency practitioner will determine his/her hourly rates for an engagement taking into account a number of factors including size of the practice, overheads, size of the engagement, difficulty of the engagement. Each firm and each engagement is different making the determination of market rates difficult. Arguably, what the market is prepared to pay is the market rate.

Amendment required

The IPAA suggests that the factor in respect of market rates of remuneration be removed.

3.1.3 The factors "may" be considered by the Court rather than "must" be considered by the Court.

Rationale

The Court should be able to exercise discretion when deciding which factors are relevant to their consideration of a practitioner's fee application.

Amendment required

The word “must” should be changed to “may” in section 425, 449E, 473 and 504.

3.2 Drafting

3.2.1 The first factor in each of the relevant sections (s 425, 449E, 473 and 504) should be amended to read – “the extent to which the work performed, or likely to be performed, by the IP was or will be reasonable necessary.”

4. Allow a fixed amount of fees to be drawn down where a creditors meeting lacks a quorum (ES p38)

4.1 Principles

4.1.1 This process for approval of remuneration should also be available in a Creditors' Voluntary Liquidation.

Rationale

Creditors' Voluntary Liquidations ("CVL") will become more popular with the change to the process of commencing CVLs. There will be instances where the liquidator will be unable to get a quorum to attend a meeting to approve his/her remuneration. As such, it is appropriate that liquidators of CVLs have access to a similar provision.

Amendment required

Proposed provision 473(4) should also be included in section 499.

4.1.2 There should be an alternative means of seeking approval of remuneration without having to hold a meeting of creditors.

Rationale

The Bankruptcy Act provides for an alternative to holding a meeting of creditors commonly known as a "flying minute".

Section 64ZBA of the Bankruptcy Act enables single proposals to be put to creditors and resolved without a meeting of creditors. The Trustee may at any time put a proposal to the creditors by giving them notice under this section. It provides that:

(2) The notice must:

(a) contain a single proposal; and

(b) include a statement of the reasons for the proposal and the likely impact it will have on creditors (if it is passed); and

(c) be given to each creditor who would be entitled under section 64A to receive notice of a meeting of creditors; and

(d) invite the creditor to either:

(i) vote Yes or No on the proposal; or

(ii) object to the proposal being resolved without a meeting of creditors; and

(e) specify a time by which replies must be received by the trustee (in order to be taken into account).

(3) If, within the time specified in the notice:

(a) at least 1 creditor votes in writing; and

(b) no other creditor objects in writing to the proposal being resolved without a meeting of creditors;

then the following provisions have effect:

(c) if the proposal requires a special resolution and there is a Yes vote by a majority in number, and at least 75% in value, of those who voted within the

required time - the proposal is taken to have been passed by a special resolution of creditors at a meeting;

(d) if the proposal does not require a special resolution and there is a Yes vote by a majority in value of those who voted within the required time - the proposal is taken to have been passed by a resolution of creditors at a meeting;

(e) in any other case - the proposal is taken not to have been passed.

This approach is consistent with recommendation 21 of the Parliamentary Joint Committee on Corporations and Financial Services report on "Corporate Insolvency Law: A Stocktake" ("PJC Report"), and the Governments response to this recommendation.

This provision should be available as an alternative to holding a meeting to more cost effectively deal with any single particular matter, including remuneration, in Court Liquidations and CVLs.

Amendment required

A provision similar to section 64ZBA should be included in the Corporations Act for use in both Court Liquidations and Creditors' Voluntary Liquidations.

This provision should be able to be utilised to deal with any single particular matter (eg remuneration, creditor approval of matters under section 477(2A) or section 477(2B)).

If this recommendation is accepted, proposed section 473(4) will need to be amended to also provide for situations where the liquidator cannot get at least one creditor to respond to the "flying minute".

4.2 Drafting

4.2.1 The $5,000 limit should be indexed in addition to providing for increases as provided for in the regulations

4.2.2 The $5,000 amount should be expressed as exclusive of GST.

5. Advertising Requirements (ES p40)

5.1 Drafting

5.1.1 The IPAA suggests that an amended version of the Form 529A (Notice of First Meeting of Creditors of company under administration) be used for the advertisement so that only date, time and place of meeting need to be provided. The significant amount of additional information that currently has to be provided results in a large increase in the cost of the advertisement.

6. Pooling in a Voluntary Administration (ES p53)

6.1 Principles

6.1.1 One creditor being able to prevent the pooling determination being made makes the proposed system less effective

Rationale

Currently administrators can seek to pool a group of companies in a Voluntary Administration by taking a vote of creditors at the second meeting in respect of proposed "Pooling Deeds". These resolutions are passed by a simple majority. Some administrators seek the approval of the Court for the pooling arrangement under section 447A, some choose not to.

The proposed system for pooling uses an objection approach with one creditor's objection preventing the administrator from making the pooling declaration.

Notwithstanding that the administrator has significant scope to create a pooling arrangement that is more likely to be accepted by creditors, the fact that it only takes one creditor to object to the arrangement to overturn it makes the process less effective and unlikely to be utilised by administrators than the current system.

The IPAA suggests that the objection process be the equivalent of a special resolution. For example, as long as more than 50% in number and 75% in value do not object, the pooling determination can proceed.

Furthermore, there is concern amongst the profession that the proposed one creditor objection process will taint the Courts consideration of pooling applications using the existing system which requires a simple majority.

It is our opinion that the introduction of a statutory mechanism for pooling has merits, however, unless the proposed system of one creditor objection is changed, there will be limited practical benefit as it will not be used. It is the IPAA's opinion that if the one creditor objection system is not changed, the proposed system should not be introduced for Voluntary Administrations and Deed of Company Arrangement.

The changes we have suggested in relation to the one creditor objection system for pooling in voluntary administrations will be equally applicable to liquidations.

Amendments required

Amendments will be required to proposed sections 442K and 574.

6.2 Drafting

6.2.1 Proposed sections 442T(2) and 442U(1)(a)– there is no point to these subsections as they refer to resolutions passed at the 439A meeting and determinations only come into force once a DOCA is signed (s442G).

6.2.2 Proposed section 548A – The IPAA agrees with the wording of this section but we do not understand why it is different in principle to the current s 548A. There is no mention of members in the proposed s 548A. We suggest that section 548 is amended to bring it in line with 548A.

6.2.3 Currently application to the Court is the only way to vary a determination. The IPAA suggests that the Voluntary Administrator / DOCA Administrator / Liquidator be able to seek creditor consent in the same way as the original determination was approved.

6.2.4 The IPAA recommends that the external administrators of pooled groups of companies be able to comply with statutory reporting requirements on a pooled basis (ie section 438D, 476 and 533 reports)

6.3 Unresolved Questions

6.3.1 What is the position of the ATO (or any other creditor in the same position) if they have a debt that each of the companies in the proposed pool are already jointly and severally liable for prior to pooling?

6.3.2 What is the position of a creditor that may hold guarantees from a number of the creditors in the proposed pool?

6.3.3 When does a pooling determination come into force if the companies are already subject to DOCAs? If companies are in VA, determination comes into force when DOCAs signed (s 44G(2), however, there is no corresponding provision if the companies are already subject to a DOCA.

6.3.4 To vary a DOCA under section 442P(3) or 442P(4) will the Deed Administrator need to call a meeting of creditors to approve the variation? Or does the Deed Administrator have the power to vary the DOCA to give effect to the variation? What are the lodgement requirements in relation to a varied DOCA?

6.3.5 There are no lodgement requirements if a variation to a pooling determination is obtained – since the original pooling determination is required to be lodged it would seem logical to have any alterations to that declaration also lodged (same issue for VAs/DOCAs and Liquidations).

6.3.6 Does the term “wound up” include Provisional Liquidation for the purposes of proposed section 539(7)(d), 572(1) and 576(1)? It is the IPAA’s opinion that it should.

6.3.7 Proposed section 571 refers to an eligible unsecured creditor as one "who, under the regulations, is entitled ..." – what regulation is referred to here?

6.3.8 When does a determination in a liquidation come into force (s 572)?

6.3.9 Proposed section 578(1)(e) may override the current process of liquidators being able to nominate an alternative to chair the meeting under regulation 5.6.17. This is not appropriate.

6.3.10 No requirement to lodge a pooling determination if the Court makes orders in a liquidation under s 576. This is inconsistent with the requirements for VAs/DOCAs.

6.3.11 Does there need to be specific mention about the right of the VA / Deed Administrator / Liquidator to be able to draw fees from the pooled funds?

6.3.12 Has consideration been given to the impact of the Debt Forgiveness Provisions contained in the Income Tax Assessment Act in respect of the extinguishment of inter-company debts?

6.3.13 Has any consideration been given to the situation where companies may be grouped for GST purposes but a different group of companies are pooled under the proposed reforms?

6.3.14 External administrators should be able to advertise on a combined basis. There is currently no mention in the reforms.

6.3.15 Some IPAA members question the need for law reform in this area. While the majority of IPAA members are practitioners and lawyers, we have an important lending constituency.

During the meetings referred to in the Introduction, some from this constituency expressed views that were not supportive of the proposed reforms. They firstly questioned their utility, noting that as a practical matter pooling in administration can be achieved under the present law, although the extent of Court involvement in the process would appear to differ between the states and territories. They secondly raised the concern that lenders particularly may be prejudiced by a pooling determination, given that the lending may be structured so that the lender does not have security or guarantees from each group company, noting that even if there is an objection by them, their views may be overridden by the Court which may impose its own views about the adequacy of the bank's existing position, and its dilution as new debts are added to those of an individual group company to which a loan is made.

7. Prescribed Disciplinary Bodies (Item 1 of Schedule 2 Regulations)

7.1 Principle

7.1.1 The IPAA should be included as a body with which ASIC can share confidential information

Rationale

The IPAA is the peak professional body for insolvency practitioners and we believe that it is appropriate that the IPAA be included along with the ICAA, CPA and NIA as bodies with which AISC can share confidential information if ASIC are satisfied that particular information will enable or assist these bodies to perform one of its functions.

Amendment required

The IPAA needs to be added to new regulation 8AA in the Australian Securities and Investments Commission regulation 2001 as a prescribed professional body.

8. Mandating the priority debt ranking in deeds of company arrangement

The IPAA has previously expressed its concerns with the potential implications of this provision. We recognise the government's policy imperative is to protect employee entitlements. The suggestions below is to ensure that implementation of the provision is efficient and effective.

8.1 Principles

8.1.1 There needs to be a requirement for administrators to provide information to employees prior to employees voting to accept a DOCA which amends the section 556 priorities.

Rationale

There needs to be a positive requirement on administrators to provide information to employees to assist them in their decision making about whether to accept an amendment to the section 556 priorities.

It is possible that the meeting of employees will be held to consider the amendment to the section 556 priorities prior to the section 439A report being issued. Even if the section 439A report is available, the information that employees will require will be different to that provided to the general body of creditors.

The IPAA will be considering the provision of guidance to our members on what information should be provided to employees, however, there should be a positive obligation under the Act which our guidance will build upon.

Amendment required

A provision should be added to new subsection 444DB requiring administrators to provide information to employees to enable them to make an informed decision about amending the section 556 priorities.

8.1.2 There should be guidance provided to the Court on what factors to take into account when comparing outcomes of a proposed DOCA which varies the section 556 priorities and liquidation.

Rationale

Specifically, the IPAA is of the opinion that there should be guidance for the Court on whether the Court is required to take into account payments that employees may be entitled to receive under GEERS if the company were to go into liquidation. Whether a Court will factor in the effect of possible entitlements under GEERS will substantially affect the comparison of outcomes.

Amendment required

A provision should be added to new subsection 444DB setting out the factors that the Court should consider. Alternatively, guidance could be provided in the Explanatory Statement.

9. SGC and Double Payments (ES p29)

9.1 Principle

9.1.1 External Administrators should be given the power to offset late payments of superannuation against the ATO's proof of debt for SGC.

Rationale

Currently only late superannuation payments made within one month of the due date will offset against the SGC debt. Although this may be appropriate leeway for solvent entities, in an insolvency scenario the offset should not be subject to a time limit which may result in employees receiving payment of their superannuation twice to the detriment of the general body of creditors.

Amendment required

The IPAA suggests that the proposed provisions dealing with double proofs (proposed sections 444DC and 553AB) be extended to also allow the insolvency practitioner to offset any late payments of superannuation made pre-appointment against any SGC proof so that only the balance beyond what has already been paid by the company is provable.

10. Creditors to have power to appoint a different person as liquidator (ES p34)

10.1 Principle

10.1.1 There is a need to balance the rights of creditors with the need to allow an administrator to do his/her job without undue pressure.

Rationale

Many practitioners have raised with the IPAA concerns that the ability for creditors to be able to appoint a different person as liquidator if they choose when a company proceeds from Voluntary Administration to liquidation may create tensions for administrators when trying to undertake the engagement. For example, if a creditor does not want an administrator to take a particular course of action, the creditor could use the threat of replacement to manipulate the situation.

The IPAA strongly believes that creditors should have the right to choose their own liquidator. We recognise that sometimes this change will occur for good reasons, such as the administrator is doing a poor job or because of a real or perceived lack of independence. However, there will also be a lot of instances where an administrator is replaced for the wrong reason, for example a creditor or creditor(s) is not happy that the administrator may have identified a potential recovery against the creditor (a preference), or lobbying by another insolvency practitioner to be appointed as liquidator.

It is our opinion that the creditors rights need to be counterbalanced to ensure the appropriate use of this provision. We suggest the following:

- It is our opinion that pressure from creditors is more likely to come from directors and related party creditors as a result of their desire to have the administrator not investigate insolvent trading, uncommercial transactions, preferences etc too closely. As such, directors and related party creditors should be excluded from being able to propose or vote on such a resolution. They would retain their right to be able to apply to the Court for a replacement liquidator.
- Subject to the appropriate approval process, the incumbent administrator's remuneration should have a priority over the replacement liquidator's remuneration. Our reasoning for this request is:
  - Administrators will naturally be concerned about the recoverability of their remuneration and if greater security is provided for remuneration, then this factor will not be available to manipulate the administrator.
  - Administrators will experience pressure to "cash up" assets to ensure that they can obtain the fullest possible protection from their lien should they be replaced.
  - Administrators may be more reluctant to take the increased risk of a decision to trade on the business if there is a chance that they will be replaced and there is unlikely to be sufficient assets covered by the administrator's lien.
  - The Administrator's lien may not always be worth anything. For example the administrator may be appointed at the same time as a Receiver with the receiver appointed under a fixed and floating charge over the whole of the company. Thus, there are no assets available to the administrator under his/her lien. There will be no assets available to the Administrator to meet his/her liabilities until such time as the company proceeds into liquidation and as liquidator he/she

takes recovery action for preferences/insolvent trading etc. If the administrator is replaced at the second meeting, he/she will be totally dependent on and subject to the actions of the replacement administrator.

- If another practitioner is requested to act as a replacement liquidator, they will give thought as to the reasons why he/she is being asked to act, rather than simply that he/she will be able to make money from the appointment, as the practitioner will need to be aware of the position of the incumbent.
- The incoming liquidator will be aware of the administrator's remuneration prior to his/her appointment and will be able to manage the costs incurred during the liquidation with this in mind. However, an administrator has no power to manage what costs are incurred by the liquidator and as such the liquidator could incur costs such that recovery of the administrator's remuneration is decreased.
- The priority for the incumbent's remuneration is still dependent on approval of that remuneration by the creditors. If the incumbent is being removed for a good reason, then the incumbent may find it more difficult to obtain approval of his/her remuneration from the creditors or the Court.

Amendments required

A provision needs to be included to exclude directors and related party creditors from proposing or voting on a resolution to appoint a different liquidator at the second meeting of creditors in a Voluntary Administration.

A subsection needs to be inserted into section 556 to grant priority for the voluntary administrator's remuneration over that of the liquidator.

11. Annual Meeting in a Creditors' Voluntary Winding Up (ES p38)

11.1 Principle

11.1.1 The timing of the Annual Meeting in a Creditors' Voluntary Liquidation ("CVL") needs to be clarified.

Rationale

A Liquidator in a CVL is required to hold an Annual Meeting of members and creditors within three months of the end of the first year from the commencement of the winding up and the end of each succeeding year (section 508).

A problem arises in CVLs that follow a Voluntary Administration due to the use of the phrase "commencement of the winding up".

Commencement of the winding up where a CVL follows a Voluntary Administration is, through the interaction of section 513B and 513C, the day on which the administration began.

Accordingly, the start date for calculating the timing of the Annual Meeting is the day on which the Voluntary Administration began. This can cause difficulties. For example, a company goes into Voluntary Administration and then executes a Deed of Company Arrangement. Some eighteen months down the track the Deed of Company fails and the company goes into Creditors' Voluntary Liquidation. Due to the length of the Deed the Liquidator has already missed holding the first Annual Meeting as it was to be held within 15 months of the day on which the administration began.

Amendment required

The IPAA proposes that the requirement for AGM's be amended so that the date to calculate the timeframe for the Annual Meeting is the first day of the liquidation, not the commencement of the liquidation.

11.2 Drafting

11.2.1 As section 508 deals with annual meetings for Members' Voluntary Liquidations and Creditors' Voluntary Liquidations, it would be more appropriate for the title of the section to be "Annual Meeting of the Company and/or Creditors".

11.3 Unresolved Questions

11.3.1 Will there be a prescribed format for the report to be lodged with ASIC?

12. Corporate Membership of the Committee of Creditors and the Committee of Inspection (ES p46)

12.1 Principle

12.1.1 Corporate creditors should still be required to appoint their representative in writing.

Rationale

The IPAA believes that it should still be a requirement that corporate creditors appoint its representative in writing, even if that representative is an officer or employee. At the moment, section 436G(2) does not require officers or employees to be authorised in writing.

It is important for the external administrator to be properly informed as to who the corporate creditor's authorised representative is. Furthermore, for the effective conduct of the Committee, it is preferable to have consistency of representation and written authorisation is more likely to encourage this consistency.

Amendments required

The IPAA suggests that proposed section 436G(2) be amended as follows:

"If a member of such a committee is a body corporate, the member may be represented at meetings of the committee by:

(a) an officer or employee of the member; or

(b) an individual

authorised in writing by the member for the purposes of the section."

13. Creditors' Voluntary Winding Up (ES p47)

13.1 Principle

13.1.1 There needs to be provisions to protect the liquidator's remuneration if they are replaced at the first meeting of creditors.

Rationale

In a Voluntary Administration the administrator has the protection of the indemnity and lien provisions. There is nothing similar to this for liquidators. If the liquidator is replaced at the first meeting, he or she has no control over what actions are taken by the replacement liquidator, including the amount of expenses and/or remuneration incurred, yet the initial liquidator's recovery of his/her remuneration and expenses is directly affected by this. It is suggested that to protect the initial liquidator's remuneration and expenses position, that the initial liquidator's remuneration and expenses are given priority over the second liquidator. The second liquidator has the protection of knowing the level of the initial liquidator's fees and expenses and the benefit of the work undertaken by the initial liquidator.

Much of the reasoning set out at point 10.1.1 is applicable here and we refer you to that discussion.

The other difficulty is that neither the initial liquidator nor the replacement liquidator will be able to be paid his/her remuneration until the conclusion of the engagement, unless the replacement liquidator is prepared to pay the initial liquidator's remuneration up front. This is because there will not be certainty of available monies until towards the end of the engagement. If there are insufficient funds on hand to meet remuneration in full, under the current system the liquidators would share pro-rata in the available monies. However, the IPAA understands that in practice what commonly happens is that the second liquidator draws his/her fees in the ordinary course and it is the first administrator whose remuneration and expenses remain unpaid until the conclusion of the engagement.

The quantum of the initial liquidator's remuneration would still need to be approved in the normal manner.

Amendment required

Section 556 needs to be amended to give a liquidator in a Creditors' Voluntary Winding Up priority for remuneration and expenses above the remuneration of any replacement liquidator.

13.2 Drafting

13.2.1 It should be the liquidator rather than the company which has to cause the meeting of creditors to be held and send notice of the meeting to creditors. The liquidator will be appointed at the members meeting.

13.2.2 Section 497(1) should state "at which the resolution for voluntary winding up is passed" rather than "at which the resolution for voluntary winding up is to be proposed". Due to the change in timeframes, the resolution will be passed before the notices are sent out. Before the changes, the notices for the creditors

meeting would have to have been sent at the same time as the members' meeting.

13.2.3 All of the references in this section are to "days" rather than "business days", it is therefore suggested that the reference to 8 business days be changed to 10 days for consistency within the section.

13.2.4 The IPAA suggests that the limit for the list of creditors in section 497(3) be increased to $1,000 and should be able to be amended in the future by regulation.

13.2.5 There needs to be amendments to section 497(8) to reflect that it is now a liquidator that is calling the meeting.

13.2.6 There is a need to amend 499 to reflect that the liquidator nominated by the company and appointed at the members' meeting is the liquidator unless relaced by the creditors at their meeting. (needs to be a provision similar to 436E(4)).

14. Change of company name in external administration (ES p 49)

14.1 Principle

14.1.1 All external administrators should have the power to apply to the Court for an exemption from the requirement to disclose a former name.

Rationale

The requirement to disclose a former name may adversely affect the ability to sell a business in any form of external administration and all external administrators should have the ability to put their case to the Court for leave not to have to disclose the company's former name.

Amendments required

Section 161A(2) and (3) will be replaced with:

"(2) Except with leave of the Court, the company must set out its former name on all its public documents and negotiable instruments"

14.2 Drafting

14.2.1 Paragraph 4.208 of the Explanatory Memorandum states that the application has to be lodged with the Court. The Bill states the application must be lodged with ASIC.

14.2.2 Section 161A(2) should refer to subparagraphs (1)(b)(i), (ii), (iii), (v) and (vi) and section 161A(3) should refer to (1)(b)(iv) if the IPAA's recommendation that all external administrators should have the right to apply to the Court for leave not to have to disclose a company's former name is not accepted.

15. Meetings

15.1 Principle

15.1.1 Administrators should be entitled to hold the second meeting of creditors in the convening period.

Rationale

There are many reasons why an administrator might wish to hold the section 439A meeting before the end of the convening period. For example, an administrator has personal liability under sections 443A and 443B for the period of the administration or it becomes apparent that the deed proposal that was being developed is not viable and the company should proceed to liquidation as quickly as possible. This position is worsened by the fact that the convening period has been extended from essentially three weeks to four weeks.

It is suggested that as long as administrators comply with their reporting and notification obligations, the administrator should be entitled to hold the second meeting of creditors at any time within the convening period or the 5 business days after the end of the convening period.

Amendments required

The IPAA suggests that section 439A(2) is amended to provide that the meeting must be held before the end of 5 days following the convening period. If felt necessary, the section could also specifically provide that the meeting can be held within the convening period.

16. Power of an administrator to sell property subject to a lien, pledge or reservation of title clause and Right of a creditor to sell property subject to a lien or pledge (ES p88 and 89)

16.1 Principles

16.1.1 The term "Net Proceeds" should be defined.

Rationale

Where an administrator or a creditor sells an asset subject to a lien, pledge or ROT they have a right to retain the net proceeds of the sale. There is currently no guidance on what net proceeds are.

It is the IPAA's opinion that the term "net proceeds" needs to be defined to give greater clarity to administrators and creditors about what costs can be offset against the proceeds from the sale of the asset.

Amendments required

The definition of "net proceeds" should be included in section 9 or in a section to which sections 442CC (administrators) and 441JA (creditors) can refer to.

16.1.2 Creditors should be subject to a reasonableness test where they are selling property subject to a lien or pledge.

Rationale

Administrators are to act reasonably when selling assets subject to a lien, pledge or retention of title clause. There is no similar requirement on creditors if they are selling an asset subject to a lien or pledge. It is the IPAA's opinion that a similar test should apply to creditors. The company has a direct interest in the sale process as it is entitled to any surplus on the sale, or alternatively the sale reduces the company's obligations.

Amendments required

A provision similar to section 442CB should be included in relation to the sale of assets subject to liens or pledges by creditors.

17. Relation-back period (ES p 92)

17.1 Drafting

17.1.1 Proposed definition of relation back date in section 9 – (ai)(iv) should read:

"that application had not been dismissed or withdrawn before the beginning of the administration that ended when the deed was executed".

As the provision is currently drafted the extended relation back date will only apply if the application to have the company wound up remained on foot until the resolution terminating the DOCA is passed. This is obviously not right – the application should only have to remain on foot until the company is placed into VA.

17.1.2 It does not appear that the scenarios set out in the proposed section 9 definition of relation-back day cover s446A(1)(b) – DOCA not signed in accordance with s444B(2); or regulation 5.3A.07 – deemed passing of special resolution to wind up in certain circumstances.

17.2 Unresolved questions

17.2.1 Do the proposed (ae), (af) and (ag) cover section 446A(2)(a)?

18. Priority of borrowings during administration (ES p93)

18.1 Principle

18.1.1 Administrators and lenders should have the right to contract out of personal liability or limit the personal liability to the value of the assets under the indemnity.

Rationale

Administrators currently make applications to the Court under section 447A to provide for personal liability for borrowings during the administration period and for the limitation of that liability where it has been contractually agreed between the administrator and the lender.

The IPAA can envisage many situations where a lender may agree to the limitation of liability (for example, existing lender wanting to provide further monies to protect their exposure, directors or related parties wanting to provide finance for the voluntary administration period). Lenders are in a different position to providers of goods and services and the law should recognise this by providing for lenders and administrators to contract out of this liability.

Amendments required

A further provision needs to be inserted into section 443A recognising the rights of lenders and administrators to contract out of personal liability.

19. Other drafting issues / Outstanding questions

19.1 SGC and excluded employees (ES p 28)

Should 64B(3A) read "if the amount of the charge payment **has** been affected by" rather than **had**?

19.2 Information to be provided to creditors to allow reasonableness to be assessed (ES p 36)

Rather than the Explanatory Statement setting a page limit, it is suggested that the explanatory statement require a simple language explanation with the number of pages provided suitable for the amount of remuneration sought.

19.3 Time limit for the lodgement of reports by liquidators (ES p64)

It is noted that the Explanatory Statement indicates a time limit running from the date of appointment, whereas the Bill states that the time limit commences when an offence is identified. There is no certainty on timing with the requirement set down in the Bill and it is preferred that the time limit commence at the time of appointment.

19.4 Notification where deed wholly effectuated (ES p73)

Are the obligations under proposed section 445FA(d) and (e) separate documents – or does the administrator prepare the document under (d) and then lodge that same document under (e)?

19.5 Power to consent to a Transfer of shares of the company (ES p 74)

Is it necessary to state who has standing to oppose a court application for leave under proposed section 444GA.

19.6 Deed Administrator's ability to sell the company's shares (ES p 76)

A Deed Administrator should be specifically given the power to alter the status of share the same as the proposed amendment in relation to liquidators and voluntary administrators.

19.7 Deed Administrator's ability to sell the company's shares

Subsection (1) requires the administrator to get the consent of the owner of the shares to a proposed transfer or the leave of the Court. If the matter goes to Court the Court is required to consider the interests of the members of the company (i.e. all members). The IPAA is of the opinion that the relevant consideration should be the interests of the owner of the shares which may differ from the interests of other members who may or may not have consented for their own reasons.

19.8 Lodgement of accounts with ASIC (ES p77)

An audit required by ASIC of an administrators' account is to be an expense of the Administration. As it is ordered by ASIC and the Auditor reports to ASIC presumably ASIC pays and then seeks reimbursement. Is this an expense covered by the administrator's indemnity? The IPAA is concerned that it may not be and as such this matter requires clarification. If there is a shortage of funds there may be an issue between ASIC and the Administrator as to who takes priority and this should be addressed through sec 556.

19.9 Report as to affairs (ES p96)

The IPAA agrees that a liquidator should be able to request a RATA from any officer of the company, including former external administrators, following a period of administration of a DOCA. However, the report should not be able to be requested for a date prior to the appointment of the initial voluntary administration. A RATA is required to be prepared by directors at the commencement of the Voluntary Administration and it would be unreasonable to require a voluntary administrator or deed administrator to complete a RATA for a date prior to their appointment.

19.10 Section 443D(a)

Existing section 443D(a) continues to refer to "subsection 443BA(3)". There is no such subsection and presumably the reference should be to "subsection 443BA(2)".

19.11 Section 443DB

This section is to be inserted before section 443E, yet there is no section 444DA in the Act as it stands or in the Bill.

19.12 Disclosure of the reasons for casting vote (ES Item 22 Regulations)

There is some concern that in some instances, reasons for the exercise of a casting vote may be considered defamatory or slanderous by parties involved. For example, if an administrator uses his casting vote against a proposed Deed of Company Arrangement and his reasoning is that he doesn't think that the directors are capable of managing the company and meeting the obligations under the Deed. This type of comment may be considered slanderous by the directors involved.

The IPAA notes that sections 442E and 535 provide Administrators and Liquidators with qualified privilege for oral or written statements. On the basis that these provisions will protect Administrators and Liquidators, the IPAA has no objection to the amendment.

20. Additional Matters for this Reform Package

20.1 Chairing of the Second meeting in a Voluntary Administration

The Corporations Regulations currently provide that where a meeting is convened by an administrator of a company under administration the meeting must be chaired by the administrator or a person nominated by that person (regulation 5.6.17(1)). However, the Corporations Act states that at a meeting convened under section 439A (the second meeting of creditors in a Voluntary Administration) the administrator is to preside (section 439B).

Due to the operation of Regulation 5.6.11(3)(c), where regulation 5.6.17 is inconsistent with a particular requirement of the Act, the regulation does not apply. Accordingly, it appears that for section 439A meetings, the administrator must chair the meeting.

It is the IPAA's opinion that this requirement is impractical. If for some reason the administrator is unable to attend the meting (for example due to ill health or an accident) the meeting is technically unable to be held. It is also unable to be adjourned. There is some concern that the Courts may not necessarily be prepared to make an order allowing an alternative chair – and in many circumstances this approval may not be able to be sought until after the meeting is held.

The IPAA recommends that section 439B be amended to provide for a representative of the administrator to chair the meeting where the administrator is unable to. The IPAA suggests that to ensure the integrity of this process, a nominee be approved by a resolution of creditors. Before creditors vote, the alternate nominee must provide creditors with details of experience and knowledge of engagement. If creditors do not approve the nominee then the meeting is automatically adjourned for 7 days. This adjournment should be separate to the 60 days adjournment available under s439B – ie. If a meeting is adjourned under s 439B and when the meeting is reconvened, if the administrator is not available then approval of the nominee is subject to creditor approval and if not accepted the meeting is adjourned for a further 7 days. This would give time for the administrator to be present at the meeting or for an application to be made to the Court to approve the use of a representative.

We note that there are concerns about the need for the administrator to personally conduct such an important meeting, however, there will be instances where the need for delegation is unavoidable. The administrator still retains ultimate responsibility for the conduct of the administration.

With disciplinary actions finding joint administrators responsible for the actions of their co-appointees, appointments of two administrators jointly and severally to a company are less common. These findings mean that each administrator must be fully informed as to the conduct of the engagement, which is not viable or cost effective for all engagements. There are also many practitioners that operate as sole-practitioners and do not have a partner to accept joint appointments with. As such, this is not a viable alternative to ensuring that there will be an administrator available to chair the meeting.

20.2 Provisional Liquidators Remuneration

If a provisional liquidation is followed by a liquidation, then the provisional liquidator should be able to first refer his/her fee approval request to creditors. As such, subsection 473(2) should be the same as 473(3).

When a company is in liquidation, the creditors are the principle stakeholders in the process and as such, they are an appropriate body for the provisional liquidator to seek approval of his/her fees from.

Should the company not proceed into liquidation, then it is appropriate that it is the Court that considers the remuneration application.

20.3 Superannuation on dividends of pre-appointment employee entitlements

It has recently come to the IPAA's attention that it is the ATO's opinion[1] 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, superannuation or any other additional obligations (eg. Payroll tax) relating to pre-appointment entitlements is a pre-appointment debt that is provable in the external administration.

[1] Copy attached

20.4 Options for directors under 222AOE notices

If a director is served with a notice under section 222AOE of the Income Tax Assessment Act 1936 they have four options to avoid personal liability:

i) the liability is paid; or
ii) an agreement to repay the debt is entered into; or
iii) the company is under voluntary administration; or
iv) the company is being wound up.

A the moment, Voluntary Administration is a very commonly used option as often the company is not in a position to repay the debt and it is unlikely that the company can be placed into liquidation in sufficient time to meet the notice's requirements.

When a company is in Provisional Liquidation it is not being wound up. As such, Provisional Liquidation does not satisfy the requirements of a 222AOE notice.

The amendments proposed in Items 1 and 2 to Schedule 4 of the Bill will confirm that when a company is in Provisional Liquidation, the directors will not be able to appoint an administrator.

As such, the IPAA is concerned that if directors of a company that is in Provisional Liquidation receive a section 222AOE notice, options (iii) and (iv) are not going to be available to them, unless the winding up application happens to be heard within the requisite timeframe.

It is not reasonable that directors are not able to access a range of options for dealing with 222AOE notices where a provisional liquidator has already been appointed. Nor is it reasonable that they can remain exposed to personal liability when an external administrator has been appointed and they are no longer in control of the company.

The IPAA recommends that section 222AOE of the Income Tax Assessment Act 1936 be amended to include at item (v) that the company has a Provisional Liquidator appointed. To address any concerns about the control of the company returning to the directors without having a liquidator appointed, the section 222AOE notice should reactivate in this event.

21. Further matters to consider looking forward

Although the following issues may not form part of the current Bill, the IPAA would like to raise them as issues for further consideration going forward.

21.1 On-line Advertising

It is the IPAA's strong opinion that further consideration should be given to the issue of moving advertising for Chapter 5 Administrations to an on-line forum.

Online advertising at one designated website will be more cost effective and readily accessible by more people. Currently advertisements placed in a newspaper are only available on the day of advertising, are not searchable and are placed in a variety of sources. All of these factors mean that it is very difficult for the target of the advertisements to actually benefit from these advertisements. Whereas, if advertisements are available online, the information will be retained for a longer period and will be fully searchable.

We are aware of concerns about equity of access and suggest that there would be ways of ensuring that the placements of advertisements online can be bought to the attention of the wider population. For example, an advertisement could be placed each business day in the relevant newspaper advising notices lodged since the last advertisement.

21.2 Insolvent trading provisions

The IPAA is concerned that Australia's tough insolvent trading laws may be discouraging the informal restructuring of viable businesses.

We have received advice that lenders to Australian businesses are looking for a process where distressed businesses can be restructured without a formal insolvency process and the wholesale destruction of stakeholder value occurring. At this point in time this has not been possible in Australia because of the risk of personal liability for insolvent trading under the Corporations Act.

The IPAA would like consideration to be given to amending the insolvent trading provisions to recognise the role of a qualified and registered restructuring professional. This may well be a matter which should be referred to the Corporations and Markets Advisory Committee for further consideration.

21.3 Improved use of electronic communication

Recommendation 20 of the PJC Report recommended that the Government consider making technology and e-commerce options more widely available to enhance communication with stakeholders in external administrations and reduce the costs of external administrations. The Government in its response to the report supported this recommendation.

The IPAA recognises that the Bill does introduce a system for electronic communication with creditors, however, it is the IPAA's opinion that the proposed system will not be effective for the following reasons:

- There is little incentive for creditors to elect to receive electronic communications;
- If only some creditor elect to receive information electronically, the external administrator will have the added burden of sending some information electronically and some in paper form;

- Electronic addresses such as email are usually person specific and if that person leaves then emails may not be received; and
- What is the external administrator's obligation if a "Cannot be delivered message" is received in response to an email?

The IPAA prefers a system such as that approved for use in the Ansett Administration. This would provide for reports to be available online and for the external administrator to send a one page notification to creditors regarding the availability of the document online. Creditors would also be provided with a phone number that they could call if they required a paper version of the report to be sent to them. Creditors would have to be notified each time a document was available online. The use of this process would be elective and external administrators would have to decide whether it was appropriate to use this process each time they communicate with creditors. If there were concerns about sensitivity of the information contained in the report, or the report was only short, then the external administrator may decide to send the full version of the report to creditors.

21.4 Moratorium on contracts in a Voluntary Administrations

Recommendation 55 of the PJC report recommended 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. The Government in its response to the report rejected this recommendation.

The IPAA is a supporter of the PJC's recommendation and request that the government reconsider its position in relation to this recommendation.

It is the IPAA's opinion, based on the experience of its members, particularly in larger Voluntary Administrations, that to achieve the objectives of Part 5.3A, an Administrator needs to have the right to continue with contracts– not have a decision made by the other party to the contract. The other party to the contract would be protected by the fact that the matter must be dealt with by the Court and the requirement that the Court be satisfied that the contracting party's interests will be adequately protected.

21.5 Status of shareholder claims (Sons of Gwalia decision)

Implication of the High Court Decision in the Sons of Gwalia

1. We are supportive of the speedy reference to CAMAC
2. Unlike ordinary creditor claims for loans, and the supply of goods and services, claims by shareholders entail:
   - Proof of misleading or deceptive conduct by the company, or some other wrongful act, including a breach of its continuous disclosure obligations AND
   - That this has caused the shareholder's loss, which usually requires the shareholder to show that they relied on the company's conduct.

     This will then require detailed legal and forensic analysis by specialists advising liquidators on the individual circumstances of every shareholder who makes a claim.

3. The consequences of the case are significant and in summary are:
    - The cost burden could be enormous reducing the pool available for distribution
    - The dividend to unsecured creditors will be greatly diluted
    - Insolvencies will be further delayed
    - Creditors are different in nature to shareholders who take the risk and reward of corporate performance
    - Shareholders have remedies directly against the Directors
    - Time is of the essence as there are several high profile liquidations that will be significantly impacted.
4. There is concern that all shareholders (not just purchasers) who retained shares because of their belief that the market was informed would also have enhanced priority.
5. Any delay by CAMAC will see significant funds spent on court cases and extensive delays of distribution. Any potentially affected liquidation may have all distributions frozen.