



**ASIC**

Australian Securities & Investments Commission

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26 February 2007

Mr David Sullivan  
The Secretary  
Parliamentary Joint Committee on Corporations and Financial Services  
Suite SG.64  
Parliament House  
CANBERRA ACT 2600  
**By email: [corporations.joint@aph.gov.au](mailto:corporations.joint@aph.gov.au)**

Dear Mr Sullivan

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

Thank you for inviting ASIC to make a submission to the above Inquiry.

We note that many of the recommendations of the Committee's June 2004 report *Corporate Insolvency Laws: a Stocktake* that are the subject of the Inquiry are policy matters for the Government to determine. We do not propose to comment on those recommendations.

Our comments on those recommendations directed towards ASIC are set out in the attached table, marked Annexure A. The recommendations addressed are: 8, 18, 24, 30, 35, 37, 40 and 41.

To further assist the Committee, an update on some of ASIC's key insolvency initiatives is provided below.

### ***Increased focus on insolvency***

Since 2002, ASIC has given greater priority to insolvency, as we focus on reducing insolvent trading and phoenix companies, and, more specifically, encouraging directors and officers of financially troubled companies to act promptly and in the interests of

creditors. In support of this increased focus, in 2002, we initiated our national external administrator assistance program and created our National Insolvency Coordination Unit. The visibility, range and impact of ASIC's insolvency activities has increased each year since 2002, such that it is now a significant national regulatory priority for the Commission.

### ***National insolvent trading program***

Our national insolvent trading program was established in July 2003, to review companies suspected of trading while insolvent. In the 2003 Budget, the Federal Government allocated \$12.3 million to allow this work to continue over the following four years.

A key aim of the program is to make directors focus on the solvency of their companies and take action sooner, rather than later, where solvency problems exist. Early action maximises the chances of the company surviving, which in turn minimises the hardship to creditors and the costs to the Australian economy caused by insolvent trading.

Directors have an obligation to inform themselves of their company's financial position and to ensure the company does not trade while insolvent. Through this program, ASIC encourages them to seek proper accounting and legal advice to ensure these obligations are not breached.

In the program's first three years (to 30 June 2006) we have undertaken surveillances of 1673 companies. Over 13% (229) of these companies had an external administrator appointed following our visit. More importantly, many positive outcomes, ranging from companies seeking professional advice or obtaining an accurate financial position, through to restructuring, refinancing or raising further capital, have been achieved through our visits.

So far this financial year (to 31 January 2007) we have visited 252 companies, of which 34 subsequently had an external administrator appointed.

### ***National external administrator assistance program***

The national external administrator assistance program was established in July 2002. This program assists external administrators by taking action against company officers who refuse to cooperate with external administrators.

Between 1 July 2002 and 30 June 2006, 1659 company officers have been prosecuted for 2892 external administrator assistance type offences, such as failure to deliver reports as to affairs, failure to deliver books and records, and failure to attend on an external administrator. These prosecutions have resulted in the courts awarding over \$2.7 million in fines and costs

This financial year, as at 31 January 2007, we have prosecuted 251 company officers for 492 external administrator assistance type offences. Fines and costs of \$615,803 have been awarded.

Importantly, around 70% of company officers contacted by ASIC now choose to comply with their legal obligations without the need for prosecution, compared to 57% at the end of the program's first year.

### ***Registered liquidator portal***

In mid 2005, we completed our three year project to deliver online lodgement of external administration forms, when the final group of forms went 'live'. Registered liquidators can now lodge all external administration forms (30 forms) online through ASIC's Registered Liquidator portal.

During the project, two series of seminars were held around the country, providing information on lodging online. One-on-one coaching was also provided for registered liquidators and a client manager appointed.

### ***Policy and guidance***

ASIC has worked over the past few years to update existing policy to provide greater guidance and clarity for external administrators.

We issued our new policy statement on liquidator registration and the ongoing requirements for maintaining that registration, Policy Statement 186 *External Administration: Liquidator registration*, on 30 September 2005.

In May 2005, ASIC issued a guide *External administration: Deeds of company arrangement involving a creditors' trust*. A creditors' trust in a deed of company arrangement is a mechanism used to accelerate a company's exit from external administration. To date, it has been used most commonly (but not exclusively) in connection with the rehabilitation of public companies listed on the ASX. In some cases, this leads to a 'backdoor listing'. Use of this mechanism often enables additional value to be obtained for the creditors of the company. However, in some circumstances a creditors' trust can lead to loss of creditors' rights. Our guidance is intended to ensure creditors' trusts are used in appropriate cases and with appropriate disclosure.

We have also:

- Issued Interim Policy Statement 174 *Externally administered companies: financial reporting and AGMs* (June 2003).
- Reissued Practice Note 50 *External administrators: lodging and reporting* (December 2002).
- Amended Policy Statement 33 *Security deposits* to reflect the reduced professional indemnity insurance requirements of the Institute of Chartered Accountants in Australia (June 2003) and to extend the policy to public practice members of the National Institute of Accountants (June 2004).

Copies of this policy and guidance can be obtained from [www.asic.gov.au/insolvency](http://www.asic.gov.au/insolvency).

ASIC will be releasing a consultation paper on its proposed guidance on external administrator remuneration in March 2007.

### ***Insolvency information sheets***

In December 2005, we released 9 information sheets that increase the awareness of company insolvency procedures among directors, employees, creditors and shareholders.

The information sheets give people who may be affected by a company's insolvency a basic understanding of liquidation, voluntary administration and receivership. They are an important step towards ensuring the wider community are well informed about insolvency laws and processes and their rights and responsibilities.

The Insolvency Practitioners Association of Australia (IPAA) has endorsed the information package and a co-badged ASIC/IPAA list of the information sheets is available for insolvency practitioners to give to people affected by a company's insolvency early in an external administration.

The information sheets, available from [www.asic.gov.au/insolvencyinfosheets](http://www.asic.gov.au/insolvencyinfosheets), are:

- Insolvency: a glossary of terms
- Voluntary administration: a guide for creditors
- Voluntary administration: a guide for employees
- Liquidation: a guide for creditors
- Liquidation: a guide for employees
- Receivership: a guide for creditors
- Receivership: a guide for employees
- Insolvency: a guide for shareholders
- Insolvency: a guide for directors

### ***Liaison with the profession***

ASIC holds regular liaison meetings with the IPAA. Regular meetings are also held with leading liquidators and senior insolvency lawyers who are members of the Institute of Chartered Accountants in Australia, CPA Australia or the Law Council. Since these current liaison arrangements were put into place in October 2002, we have held 45 liaison meetings with members of the profession, and 9 liaison meetings with the IPAA. (We also have held ad hoc meetings on specific topics with members of the IPAA Board and other insolvency practitioners.)

As stated above, ASIC held workshops across the country in 2002 and 2005 to provide information to practitioners and their staff on lodging electronically on-line through the Registered Liquidators portal, as well as to discuss other ASIC insolvency initiatives. In October 2004, we held seminars throughout Australia to discuss our Liquidator Registration policy proposal paper.

### ***Assetless Administration Fund***

The Assetless Administration Fund ('the AA Fund') finances preliminary investigations and reports by liquidators into the failure of companies with few or no assets, when it appears to us that we may be able to take enforcement action as a result of their investigations and reports. In October 2005, the Federal Government announced funding to ASIC of \$23 million over 4 years to establish the AA Fund and undertake follow-up action.

ASIC launched the AA Fund on 22 February 2006, with the release of our *Assetless Administration Fund: Funding criteria and guidelines* for Stage 1 of the fund. Stage 1 involves funding liquidators to investigate and prepare supplementary s533 reports when s206F director disqualification proceedings (banning proceedings) may be appropriate.

In May 2006, the *Assetless Administration Fund: Funding criteria and guidelines* were reissued with the launch of Stage 2 of the AA Fund. Stage 2 extends to funding liquidators to undertake detailed investigations and prepare comprehensive supplementary section 533 reports where other (i.e. non administrative banning) enforcement action for breaches of the Act may be warranted.

Since the AA Fund was launched, ASIC has approved 164 applications for funding of investigations and reports on potential director banning matters (Stage 1 matters).

Already liquidators' reports funded by the AA Fund have led to the banning of 30 directors for a total of 107 years. These directors engaged in misconduct associated with company failures and repeat phoenix activity.

We currently have another 56 potential banning matters in progress using information in funded liquidator reports.

ASIC has also approved 10 applications for funding for reports on potential breaches of the *Corporations Act 2001* that may warrant civil penalty proceedings or criminal prosecution (Stage 2 matters). The potential breaches involved in these applications include:

- breaches of directors' duties
- insolvent trading
- fraudulent phoenix activity
- managing a company while disqualified.

Criminal and serious civil matters generally take some time to come to court. It is premature for ASIC to comment on any action we have taken or may take arising from these applications.

### ***Director bannings under s206F***

In 2006, ASIC banned 46 directors for a total of 174.5 years. This figure includes 17 cases where liquidators were funded by the AA Fund to investigate and prepare reports. (These numbers are slightly higher than those referred to in ASIC's response to the

ANAO report because that response was sent on 18 December 2006, and a further 3 directors were subsequently banned for a total of 11 years.)

***Conclusion***

ASIC's submission has addressed those recommendations of the Committee's 2004 report that are the subject of this inquiry which are directed specifically to ASIC. It has also highlighted some of ASIC's key insolvency activities and results.

ASIC would welcome the opportunity to discuss further the issues raised in this submission.

Yours sincerely

A handwritten signature in black ink that reads "Malcolm Rodgers". The signature is written in a cursive, slightly slanted style.

Malcolm Rodgers  
Executive Director, Regulation

**ASIC SUBMISSION TO PJC INQUIRY INTO THE EXPOSURE DRAFT OF  
THE CORPORATIONS AMENDMENT (INSOLVENCY) BILL 2007 AND RELATED DRAFT REGULATIONS**

**February 2007**

\* Throughout this table, references to 'the Act' are to the *Corporations Act 2001* (Cth).

No	PJC Recommendation	ASIC Comments*
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.	<p>ASIC takes account of the quality of RATAs provided by directors to the extent permitted by the Act.</p> <p>The external administrator is generally in the best position to assess the quality or adequacy of information provided in a RATA. ASIC may receive complaints from external administrators about:</p> <ul style="list-style-type: none"> <li>▪ failure by directors to provide a RATA; or</li> <li>▪ provision of an inadequate RATA.</li> </ul> <p>Some external administrators have power to send a director a notice requesting specific information if they believe that there has been a material omission in a RATA (e.g. s430(1) and s475(2) of the Act). We understand that external administrators often rely on these notice provisions to obtain better information from directors. Under the Exposure Draft of the Corporations Amendment (Insolvency) Bill 2007, it is proposed to extend this notice power to liquidators in a creditors' voluntary liquidation that immediately follows an administration or deed of company arrangement (proposed s446C).</p> <p>Where the appropriate evidence exists, ASIC can and does prosecute directors and other relevant persons, depending on the type of external administration, for failure to comply with an external administrator's notice requiring specific information or failure to provide reasonable assistance.</p> <p>ASIC can also prosecute directors and other relevant persons under s1308(2) of the Act if information in a RATA is false or misleading.</p>

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.	ASIC intends, in the future, to publish guidance to assist administrators in preparing their administrator's report. However, we are currently working on higher policy and guidance priorities. These include a consultation paper outlining proposed guidance on remuneration charging (see immediately below) and a consultation paper on proposed guidance on external administrator independence. ASIC will then prepare further guidance for external administrators, which will include guidance on the content of administrators' s439A reports.
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.	ASIC intends to release a consultation paper outlining proposed guidance on remuneration charging in March 2007. ASIC has consulted with the Insolvency Practitioners Association of Australia (IPAA) during its development of the consultation paper.
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.	ASIC notes that it is compiling statistics from electronically lodged statutory reports in the format of Schedule B to ASIC's Practice Note <i>50 External administrators: reporting and lodging</i> for the 2004/2005 and 2005/2006 financial years.
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.	People can already alert ASIC to potential phoenix activities by lodging a complaint. This may be done online via ASIC's website, by fax or by post. The website provides guidance for potential complainants.  Further information and assistance about lodging complaints with ASIC is available from Infoline, ASIC's telephone hot-line.
37	The Committee recommends that in its enforcement programs for the lodgement of external administrators' statutory reports, ASIC also take	As noted in the Committee's 2004 Report <i>Corporate Insolvency Laws: a Stocktake</i> (paragraphs 9.7 and 9.11), the quality of external administrators' reports is affected by the quality of the directors' RATA (see recommendation 8 above) and the state



<p>greater account of the quality of reports provided.</p>	<p>of the books and records of the externally administered company.</p> <p>In the case of liquidators, it is also affected by s545 of the Act, which provides that generally liquidators are not under an obligation to incur any expense unless there is sufficient available property to fund it. As a result, if a company is left with few or no assets, the liquidator is likely to perform only a perfunctory investigation.</p> <p>Against this background, ASIC is actively pursuing two initiatives, the Assetless Administration and the External Administrator Assistance programs, that aim to increase the quality and timeliness of statutory reports alleging offences, and thereby increase the levels of regulatory action available to ASIC to take in response to statutory reports.</p> <p>ASIC recognised the potential for a regulatory gap where the insolvent company has insufficient assets to fund the liquidator's investigation. ASIC, therefore, made submissions to Government about the need for additional funding for assetless administrations and any enforcement action that may arise from this initiative. This funding bid was successful and in October 2005 ASIC was funded \$23 million over four years to establish an assetless administration scheme. This scheme is used to fund liquidators of assetless companies so that they can properly investigate and report to ASIC on these companies. It also funds follow-up enforcement action by ASIC. Under the terms of the Assetless Administration Fund agreement with liquidators, payment for the investigation and s533 report will not be finalised until the report is of a standard acceptable to ASIC</p> <p>Our successful External Administrator Assistance Program involves ASIC pursuing compliance with company officers' obligations to produce company books and records, and to assist the external administrator in the conduct of the external administration, and if this fails, prosecuting company officers for breach of these obligations. Around 70% of company officers contacted by ASIC now choose to comply with their legal obligations without the need for prosecution. By pursuing these offences (eg. securing the production of books and records or a report as to affairs), ASIC is working with the external administrator to increase the quality of the external administrator's investigation of the company's affairs and subsequent reporting to ASIC in relation to suspected misconduct.</p> <p>ASIC also believes that the additional funding provided by the Government in</p>
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		<p>2005 will allow ASIC to increase its impact in this area going forward.</p> <p>Further information on the results achieved by the AA Fund to date and our External Administrator Assistance program is provided in the covering letter to this submission.</p>
40	<p>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.</p>	<p>See comments on recommendation 30 above.</p>
41	<p>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.</p>	<p>The Schedule B statistics currently being compiled by ASIC (referred to in our comments on recommendation 30 above) will identify the number of initial electronically lodged reports where the external administrator indicates a contravention of s286. They will also identify the number of reports where the external administrator has indicated that they have failed to obtain the books and records and the number of reports where the external administrator considers those books and records to be inadequate.</p> <p>Allegations of failure by a company to keep adequate financial records in breach of s286 and the consequent contravention by a director of the company of s344 are taken into consideration in administrative action proceedings by ASIC to disqualify directors under s206F.</p>