



Law Council  
OF AUSTRALIA

*From the Office of  
the President*

**TIM BUGG**

Mobile 0418 583 166

president@lawcouncil.asn.au

Mr David Sullivan  
Secretary  
Parliamentary Joint Committee on Corporations & 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 ("Draft Legislation")**

I write in response to your invitation by letter dated 14 December 2006 to the Law Council of Australia to provide a written submission in relation to the above inquiry.

The Insolvency and Reconstruction Law Committee of the Business Law Section of the Law Council of Australia ("**the Insolvency Committee**") is appreciative of the opportunity to make this submission.

You are probably aware that the Insolvency Committee has had the opportunity to be represented on the Insolvency Law Advisory Group assisting the Treasurer ("**ILAG**") with the Draft Legislation.

Generally speaking, the Insolvency Committee believes that the Draft Legislation is a very worthwhile improvement and development in corporate insolvency laws in this country and strongly supports its implementation.

The Insolvency Committee recognises the need to endeavour to accommodate the wishes of various stakeholders. The Insolvency Committee recognises that, as a consequence, not all of the matters which might have been included in the Draft Legislation or those which may have been the subject of your report of June 2004 have been included.

However, the Insolvency Committee does not believe that there are any matters which are so significant that the introduction and passing of the Draft Legislation should be deferred or delayed.

GPO Box 1989, Canberra,  
ACT 2601, DX 5719 Canberra  
19 Torrens St Braddon ACT 2612

Telephone +61 2 6246 3788  
Facsimile +61 2 6248 0639

Law Council of Australia Limited  
ABN 85 005 260 622  
www.lawcouncil.asn.au ADL Trans:69099.1

I also note that representatives of the Insolvency Committee have been liaising closely with the Insolvency Practitioners Association of Australia ("IPAA") both in respect of the role of IPAA in ILAG and in preparation of submissions to Treasury in respect of the Draft Legislation.

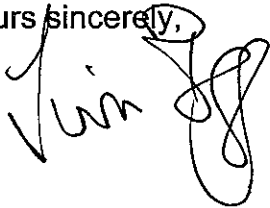
It has become apparent throughout that process that the Insolvency Committee and the IPAA share a large number of similar views on various matters relating to corporate insolvency law, its policy and reform.

I attach to this submission some additional comments addressing the specific recommendations you identify in your above letter.

I note that the Parliamentary Joint Committee intends to conduct a public hearing on 5 March 2007. If you believe it would assist, David Proudman who is the Chair of the Committee can attend. He may be contacted on (08) 8239 7118 or at [david.proudman@jws.com.au](mailto:david.proudman@jws.com.au).

I trust this submission is of assistance.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Tim Bugg', with a large, stylized flourish extending from the end of the name.

**Tim Bugg**

2 March 2007

## ADDITIONAL COMMENTS ON RECOMMENDATIONS

### CORPORATION INSOLVENCY LAWS: A STOCKTAKE – REPORT, JUNE 2004.

#### A. The Regulation of the Insolvency Process

##### Recommendation 7

*3.111 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 Insolvency and Reconstruction Law Committee of the Business Law Section of the Law Council of Australia ('the Insolvency Committee') has no objection to this Recommendation and would likely support playing a role in any advisory council so established.

##### Recommendation 8

*4.15 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 Insolvency Committee does not believe this is a matter which is best reflected in legislation and it should not delay implementation of the Draft Legislation.

##### Regulation 13

*4.60 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 Insolvency Committee does not support this Recommendation.

When a company is solvent the interests of the shareholders should prevail over the interests of creditors. When a company is insolvent the interests of creditors should prevail.

The Insolvency Committee believes that to remove the insolvency prerequisite changes the focus of the transaction (effected when the company is solvent) to one concerning the interests of creditors rather than the interests of shareholders.

### **Recommendation 33**

*8.81 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 Insolvency Committee has no objection to this Recommendation.

However, the Draft Legislation should not be delayed or deferred to incorporate this Recommendation.

### **Recommendation 35**

*8.86 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 Insolvency Committee does not consider this is a matter which should be the subject of legislative reform.

### **Recommendation 37**

*9.12 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 Insolvency Committee does not consider that this Recommendation should be the subject of legislative reform.

### **Recommendation 47**

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

The Insolvency Committee has had the benefit of reviewing the submissions put to you by the Insolvency Practitioners Association of Australia ("IPAA") dated 13 February 2007 and agrees with the comments made by the IPAA in respect of this Recommendation 47.

### **Recommendation 52**

*11.33 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 Insolvency Committee appreciates why the committee might make the recommendation contained in Recommendation 52.

However, the Insolvency Committee is of the view that any legislation which restricts the existing flexibility of deed of company arrangement proposals is something the Insolvency Committee would be disinclined to support.

## **Recommendation 54**

*12.23 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.*

The Insolvency Committee was of the view that the directors of a company ought to be in a position to appoint a liquidator by resolution of the directors in the same manner and with the same ease as directors can appoint a voluntary administrator.

The Draft Legislation requires a meeting of shareholders as well as the directors which, in our view, is unnecessary.

## **B. The Role of Administrators**

### **Recommendation 3**

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

The Insolvency Committee supports this Recommendation.

### **Recommendation 12**

*4.49 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.*

This Recommendation has been incorporated in the Draft Legislation in the sense that reports issued pursuant to section 439A of the Corporations Act are required to contain all information which is available.

The Insolvency Committee notes that the legislation is not entirely clear as to the extent to which information should be provided to employees in circumstances where it is proposed that employee entitlements are not to be treated in a deed of company arrangement proposal in a manner consistent with the statutory priorities.

### **Recommendation 24**

*7.23 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.*

The Insolvency Committee notes that there are now specific provisions in the Draft Legislation dealing with the remuneration of insolvency practitioners and that ASIC is likely to be issuing a consultation paper on the issue shortly.

The Insolvency Committee understands that the IPAA are likewise updating and reconsidering their Statement of Best Practice on this issue.

### **Recommendation 25**

*7.25 The Committee recommends that an administrator should be prohibited from using a casting vote in a resolution concerning his or her remuneration (see also recommendation 3).*

The Insolvency Committee supports this Recommendation.

Whilst the Insolvency Committee does not believe that the legislation should be delayed to address this issue, if that is to occur, any use of the casting vote in favour of their ongoing involvement (e.g. as deed administrator) should identify whether or not that constitutes exercising a casting vote "in a resolution concerning his/her remuneration".

### **Recommendation 55**

*12.34 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.*

The Insolvency Committee supports this Recommendation.

While the Insolvency Committee does not believe that the introduction of the Draft Legislation should be delayed given the omission of this Recommendation from that Draft Legislation, this is a matter which should remain on the reform agenda.

## **C. The Role of Directors**

### **Recommendation 10**

*4.23 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 Insolvency Committee supports this Recommendation but would not want it to delay the commencement of the Draft Legislation.

### **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 Insolvency Committee does not support this Recommendation. The Insolvency Committee considers that there is a distinct difference between "likely to become" and "may become".

The Insolvency Committee believes that the directors should give careful consideration to the prospects of insolvency rather than simply reach the view that the company may at some time in the future become insolvent.

### **Recommendation 31**

*8.59 The Committee recommends that ss206D 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 s206D(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 Insolvency Committee has no objection to this Recommendation but would not wish its omission to defer the Draft Legislation.

### **Recommendation 54**

*12.23 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.*

The Insolvency Committee refers you to its comments in respect of Recommendation 54 above.

## **D. The Rights of Creditors, Including the Treatment of Employee Entitlements**

### **Recommendation 43**

*10.67 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 Insolvency Committee has no objection to this Recommendation and does not regard it as a matter which should be the subject of legislative reform at this time.

### **Recommendation 44**

*10.87 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 Insolvency Committee has no objection to this Recommendation but does not believe that it should form part of the legislative reform at this time.

### **Recommendation 47**

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

The Insolvency Committee believes that this Recommendation has been incorporated in the Draft Legislation save for our comments above.

## **E. The Need for Empirical Research and Review Processes**

This section deals with Recommendations 29, 30, 32, 34, 40, 41, 43 and 58.

The Insolvency Committee has no objection to any of the Recommendations set out in the preceding paragraph.

However, the Insolvency Committee regards all such matters as falling outside of the deliberations of the Draft Legislation. The Insolvency Committee does not believe that any of the matters referred to in these Recommendations which have not been incorporated into the Draft Legislation should delay the implementation of that Draft Legislation.

Please direct any queries or concerns to David Proudman.