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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

CORPORATIONS AMENDMENT (STRENGTHENING PROTECTIONS FOR
EMPLOYEE ENTITLEMENTS) BILL 2018

EXPLANATORY MEMORANDUM

Table of contents

Glossary.....	1
General outline and financial impact.....	3
Chapter 1 Background to the reforms to address corporate misuse of the FEG scheme	5
Chapter 2 Employee Entitlements	11
Chapter 3 Contribution orders	37
Chapter 4 Disqualification from managing corporations	49

Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
AAT	Administrative Appeals Tribunal
ASIC	Australian Securities & Investments Commission
ATO	Australian Taxation Office
Bill	Corporations Amendment (Strengthening Protections for Employee Entitlements) Legislation Bill 2018
Consultation paper	<i>Reforms to address corporate misuse of the Fair Entitlements Guarantee scheme</i> consultation paper
Commencement time	The day after the Bill receives the Royal Assent.
Corporations Act	<i>Corporations Act 2001</i> (Cth)
DJSB	Department of Jobs and Small Business (DJSB)
DOCA	Deed of company arrangement
FEG	Fair Entitlements Guarantee
FEG Act	<i>Fair Entitlements Guarantee Act 2012</i> (Cth)
FEG Recovery Program	Fair Entitlements Guarantee Recovery Program
FEG scheme	Fair Entitlements Guarantee scheme
FWO	Fair Work Ombudsman
GEERS	General Employee Entitlements and Redundancy Scheme

General outline and financial impact

Enforcement and recovery related amendments to the Corporations Act to address corporate misuse of the Fair Entitlements Guarantee scheme

Schedules 2 to 4 to the Corporations Amendment (Strengthening Protections for Employee Entitlements) Bill 2018 (the Bill) make amendments to the *Corporations Act 2001* (Cth) (the Corporations Act).

The Bill strengthens enforcement and recovery options to deter inappropriate market behaviours which result in the avoidance of the payment of employment entitlements, resulting in the improper shift of some or all of these costs ultimately onto Australian taxpayers through the drain on the taxpayer funded Fair Entitlements Guarantee (FEG) scheme.

The Bill also introduces new provisions that will facilitate disqualification of company directors of two or more companies that have relied on the FEG scheme, and have also breached, or was an officer of a company that breached, the Corporations Act on at least two occasions.

Date of effect: The amendments will apply from the day after Royal Assent.

Proposal announced: On 5 October 2017, the Government announced its intention to implement law reform to address corporate misuse of the FEG scheme.

Chapter 1

Background to the reforms to address corporate misuse of the FEG scheme

Outline of chapter

- 1.1 Corporate misuse of the Fair Entitlements Guarantee (FEG) scheme by adopting sharp corporate practices is contributing to the strong upwards cost trend of the taxpayer funded scheme.
- 1.2 Corporate misuse of the FEG scheme should be deterred to ensure the burden due to the over-reliance on the scheme is relieved so that the scheme remains sustainable.
- 1.3 This chapter provides background on the corporate misuse of the FEG scheme, and why reforms to the law are required to address this misuse.

Corporate misuse of the Fair Entitlements Guarantee scheme

- 1.4 On 17 May 2017, the Government released its *Reforms to address corporate misuse of the Fair Entitlements scheme* consultation paper (the consultation paper).
- 1.5 The consultation paper outlined that certain corporate employers and associated parties are increasingly adopting a range of questionable practices that rely on the protection contained in the *Fair Entitlements Guarantee Act 2012* (Cth) for the payment of outstanding employee entitlements. Relying on these protections allows the employers to shift the cost of payment of those entitlements from their businesses to the FEG scheme, and through the scheme, to Australian taxpayers.
- 1.6 The practices adopted to shift costs onto taxpayers are broadly termed sharp corporate practices. Sharp corporate practices are a range of methods used by certain company representatives, company owners, pre-insolvency advisers, or other parties involved in corporate restructures, which seek to prevent, avoid or reduce the payment of obligations to creditors (including employee creditors and the Australian Taxation Office).
- 1.7 Sharp corporate practices also includes phoenix activity, which involves the transfer of assets from an existing company to a new company without paying fair or market value. The same business is continued under the new company, leaving any debts (such as taxes,

creditors and employee entitlements) with the existing company which is liquidated. Whilst not all phoenix activity is illegal, what separates a legitimate business rescue from illegal phoenix activity is the business operators' intentions to avoid paying debts and liabilities.

1.8 The consultation paper also noted that corporate misuse of the FEG scheme is not isolated, with the relevant sharp corporate practices occurring across most industries.

1.9 The cost of these behaviours were also found to be significant, contributing to the upwards cost trend and drain on the FEG scheme.

1.10 Average annual costs under the FEG scheme has more than tripled from \$70.7 million in the four year period between 1 July 2005 and 30 June 2009, to \$243.6 million in the four year period between 1 July 2013 and 30 June 2017.

1.11 In this context, it is important to note that the costs imposed on the FEG scheme from just a few select instances, by those attempting to avoid their employee entitlement payment obligations, equated to more than \$100 million of taxpayer funded money in the last few years.

Addressing corporate misuse of the FEG scheme using current mechanisms

1.12 While the use of sharp corporate practices are not always illegal, they place an unfair burden on Australian taxpayers where those practices result in improper reliance on the FEG scheme.

1.13 These practices hurt all hard-working Australians – including small business and sole-trader creditors through lost payments for goods and services already supplied; employees through lost wages and superannuation entitlements; and ultimately all Australian taxpayers through not only the drain on the FEG scheme, but through lost taxation revenue.

1.14 In addition, those who pursue these practices gain an unfair advantage over their honest competitor businesses who comply with their legal obligations to pay their debts, which has a broader economic impact.

1.15 Further, the use of sharp corporate practices may also significantly impede, reduce or prevent the recovery of FEG payments through the insolvency process. There are many reasons for this including that there is insufficient clarity around the circumstances and scenarios in which civil recovery provisions under section 596AC should operate and as such, relevant parties such as liquidators and employees believe the provisions are too difficult to use.

1.16 This builds on other Government actions to address these concerns, including:

- announcing law reforms to combat illegal phoenix activities; and
- introducing legislation to tackle non-payment of the Superannuation Guarantee by targeting employers that fail to meet their obligations.

1.17 Government departments and agencies have also adopted a range of administrative actions and legal approaches to assist in mitigating the impacts of sharp corporate practices on the FEG scheme and other unsecured creditors. These include:

- engaging in correspondence with relevant parties to insolvencies about the impact of certain practices and potential breaches of the law, to seek redress and ensure the Commonwealth and other employee creditors are paid what they are legally entitled to;
- undertaking recovery and legal action under the FEG Recovery Program to enforce the Commonwealth's rights in court against various parties to insolvencies;
- engaging with industry stakeholder bodies to build awareness of the prevalence of relevant practices and seek their assistance to correct misunderstandings of the law and to appropriately sanction conduct of members adopting inappropriate methods; and
- pursuing relevant matters through the Government's Phoenix Taskforce and Serious Financial Crimes Taskforce to combat illegal phoenix activity and other fraudulent corporate operations.

1.18 While this assists in mitigating the impact of some sharp corporate practices, the actions are largely targeted at illegal activities after they have occurred and will not address all of the sharp corporate practices adopted by select corporate employers, their representatives and other parties to insolvencies such as pre-insolvency advisers.

1.19 In particular, the current law does not adequately mitigate the risks and costs imposed on the community, nor does it appropriately deter or sanction the behaviours of:

- those involved in agreements or transactions which result in the intentional avoidance or reduction of the payment of employee entitlements, which results in inappropriate reliance on the FEG scheme;
- those using a corporate group structure to avoid or reduce their exposure to employee entitlement obligations which results in inappropriate reliance on FEG; and

- company officers and directors who have a history of involvement in failed companies, where FEG is repeatedly used to pay part or all of a company's outstanding employee entitlements.

1.20 To address these behaviours, enforcement focussed law reform is required. Chapters 2 to 4 of the Bill outline the specifics of these reforms to the Corporations Act.

Development of the Bill's reforms to the law

1.21 The enforcement related amendments to the Corporations Act described in Chapters 2 to 4 of this explanatory memorandum are the result of extensive public consultation processes conducted during 2017 and 2018, aimed at ensuring the reforms are appropriate and sufficiently targeted to address the corporate misuse that has been identified.

1.22 The public consultation processes included:

- releasing the Government's consultation paper on 17 May 2017, seeking stakeholder views on a number of potential options to reform the law aimed at addressing corporate misuse of the FEG scheme;
- receiving 39 submissions on the consultation paper;
- holding four stakeholder roundtable meetings in Sydney on 21 June 2017 and Melbourne on 6 July 2017, to discuss and develop the law reforms options outlined in the consultation paper; and
- further consultation in 2018 to further refine and develop the enforcement related reforms outlined in the consultation paper.

1.23 The strong feedback from stakeholders throughout the consultation processes has been that law reforms to address the corporate misuse of the FEG scheme should be made, and that those responsible for such behaviours need to be appropriately sanctioned. Stakeholders noted the reforms should target the improper behaviour without limiting legitimate commercial operations and business rescues.

1.24 The reforms to the law contained in Schedules 2 to 4 of this Bill broadly align with the options for reform outlined at Options 1, 2, 2A, 3, 4, 5 and 6 in the consultation paper, being:

- strengthening the ability of the Commonwealth to pursue recovery of FEG payments from companies, their directors,

and other relevant parties under Part 5.8A of the Corporations Act - Options 1, 2, 2A, 3 and 4;

- amending the Corporations Act to enable contributions to be sought across a corporate group in limited circumstances - Option 5; and
- enhancing measures to disqualify company directors and officers with a track record of insolvencies involving payments of FEG assistance - Option 6.

Chapter 2

Employee Entitlements

Outline of chapter

2.1 Part 1 of Schedule 1 to the Bill makes amendments to Part 5.8A of the Corporations Act to strengthen the protections provided for the recovery of employee entitlements in insolvency. This will enable the Part to operate more effectively to deter parties entering into agreements or transactions which seek to avoid the payment of, or reduce the amount of, those entitlements.

Context of amendments

2.2 The provisions of the Part were introduced into the law by the *Corporations Law Amendment (Employee Entitlements) Act 2000* (Cth) after a number of high profile insolvencies.

2.3 The Part is intended to protect employee entitlements (defined in subsection 596AA(2) of the Part) from relevant agreements and transactions that are entered into with the intention of defeating the recovery of those entitlements by:

- making it a criminal offence for persons to enter into a relevant agreement or transaction with the intention of preventing the payment of, or significantly reducing some or all of, a company's employee entitlement liabilities (section 596AB of the Part); and
- allowing a civil recovery action to be brought by the liquidator (or employees in select circumstances) to recover the loss or damage incurred by the avoidance of the payment of the employee entitlements (section 596AC of the Part).

2.4 The protected employee entitlements are the same entitlements that receive preferential payment in a corporate winding-up, as outlined in section 556 of the Corporations Act. This is a deliberate design feature of the Part.

2.5 Since its introduction into the law in 2000, there have been no successful criminal or civil court actions under the provisions of the Part.

2.6 The Government's *Reforms to address corporate misuse of the Fair Entitlements Guarantee* scheme consultation paper notes

- the current provisions in the Part are not operating effectively to achieve their intended aims; and
- reforms to improve and strengthen the Part's operation is not just desirable but necessary.

2.7 This view received strong stakeholder support.

Summary of new law

2.8 Part 1 of Schedule 1 to the Bill makes amendments to the Corporations Act to strengthen the Part's operation to ensure it achieves its policy aim of deterring the avoidance of employee entitlements and protecting such entitlements from agreements or transactions that would operate to defeat their payment or recovery.

2.9 In summary:

- the fault element necessary to contravene the criminal offence provision in the Part (section 596AB) is extended to include a person who enters into an agreement or transaction that avoids the payment of, or significantly reduces the amount of, the employee entitlements liabilities of a company which can be recovered, where the person is 'reckless' as to those possible outcomes;
- a new civil recovery provision is introduced into the Part (section 596ACA), where contravention is determined by an objective assessment of what a reasonable person would have known or been expected to have known in the specific circumstances of the case, about the relevant agreements or transactions claimed to have caused loss or damage to the company's employees;
- a new civil penalty provision is created to strengthen enforcement options for contravention of the Part (subsection 596AC(1));
- the parties who can initiate civil recovery proceedings under the Part are expanded to include the Australian Taxation Office (ATO), the Department of Jobs and Small Business (DJSB) and the Fair Work Ombudsman (FWO); and
- various drafting improvements are made to the Part to enhance its clarity, including taking the opportunity to redraft certain provisions to make them easier to understand.

2.10 As a result of the amendments, three possible actions may be available where persons are suspected of contravening the Part's requirements:

- criminal sanction for contravention of section 596AB;
 - being where a person enters agreements or transactions that are intended to avoid the payment of, or significantly reduce the amount of, a company's employee entitlement liabilities; or
 - where a person enters such agreements and transactions, and is reckless as to those possible outcomes;
- civil recovery action under section 596ACA;
 - where contravention is determined by an objective assessment of what a reasonable person would have known or been expected to have known in the specific circumstances of the case, about the relevant agreements or transactions claimed to have caused loss or damage to the company's employees; and
- civil penalty proceedings for contravention of subsection 596AC(1);
 - where contravention is determined using the same objective assessment that is used for the Part's civil recovery action.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>The current criminal offence under the Part is retained but it has been redrafted.</p> <p>In addition, the fault element necessary to contravene the criminal offence is extended to include a person who enters into an agreement or transactions that avoids the payment of, or significantly reduces the amount of, a company's employee entitlement liabilities, where the person is 'reckless' as to those possible outcomes.</p>	<p>It is a criminal offence under section 596AB of the Part for persons to enter into a relevant agreement or transaction that intentionally avoids the payment of, or significantly reduces the amount of, a company's employee entitlement liabilities.</p>
<p>The civil recovery provision in the Part (section 596ACA) is separated</p>	<p>Under the civil recovery provision in the Part (section 596AC), the</p>

<p>from the criminal offence provision (section 596AB) and no longer uses the criminal offence provision to base its operation.</p> <p>Civil recovery action under section 596ACA can be taken where persons are suspected of contravening the objective test in section 596AC (being what a reasonable person would have known or been expected to have known in the specific circumstances, about the relevant agreements or transactions which are claimed to have caused loss or damage to the company's employees).</p>	<p>company's liquidator can bring civil recovery action to recover the loss or damage incurred by avoidance of the payment, or significant reduction of the amount, of the company's employee entitlement liabilities by relevant persons.</p> <p>The civil recovery provision in Part 5.8A is dependent and intertwined with Part 5.8A's criminal offence provision (section 596AB). Breach of the civil recovery provision occurs where the criminal offence provision is contravened, but proved on the balance of probabilities.</p>
<p>The ability of employees to bring civil recovery action with the consent of a company's liquidator or the Court, is retained.</p> <p>In addition, the parties who can initiate civil recovery action under the Part is expanded to include the ATO, DJSB and FWO (section 596AF).</p> <p>As with the company's employees, the expanded parties must seek the company liquidator's consent to commence recovery action, and if this consent is not provided, can seek the consent of the Court to take action.</p>	<p>Civil recovery action can be brought by the company's former employees where they have the consent of the company's liquidator to proceed, or if permission is not granted by the liquidator, can seek the consent of the Court to take action.</p>
<p>A new civil penalty is introduced to strengthen the enforcement options for contravention of the Part (section 596AC(1)).</p> <p>Contravention of the civil penalty provision is determined using the same objective test as used to found civil recovery action.</p>	<p>No equivalent.</p>

Detailed explanation of new law

2.11 Part 1 of Schedule 1 to the Bill makes amendments to the Corporations Act to reform, modernise and strengthen the Part's operation to ensure it achieves its policy intent of deterring the avoidance of employee entitlements and protecting those entitlements from agreements and transactions that would prevent payment of, or significantly reduce the recovery of, those entitlements.

Section 596AA: Objects and coverage of the Part

Objects of the Part

2.12 Subsection 596AA(1) of the Part clarifies and restates the objects of the Part, which are:

- to deter the avoidance of the payment of employee entitlements (which are protected under subsection 596AA(2) of the Part); and
- to protect employees of companies from relevant agreements and transactions that aim to prevent the recovery of those entitlements, or which aim to significantly reduce the amount of those entitlements that can be recovered.

[Part 1 of Schedule 1, item 4, subsection 596AA(1)]

2.13 The purpose of the amendment to the objects of Part 5.8A is to:

- make it clear that the Part now has a broader scope of operation than when the Part was first introduced in 2000, including that it now operates to capture persons' actions where they are reckless as to the possibility of defeating the recovery of employee entitlements (as opposed to the previous standard, which only captured actions that were intended to defeat the recovery of employee entitlements); and
- make it explicit that the reforms to the Part are also intended to deter behaviours which would result in persons either attempting to, or being successful at, avoiding the payment of some or all of the employee entitlements, or significantly reducing the amount of employee entitlements, that can be recovered.

2.14 The heading for section 596AA is amended to reflect the amended objects for the Part. *[Part 1 of Schedule 1, item 3, section 596AA (heading)]*

Coverage of the Part

The Part potentially applies to a very broad range of scenarios

2.15 By design, the Part can apply to a very broad range of scenarios based on the facts of each case. Specific exceptions to the Part's operation are outlined in the amendments in the Bill to sections 596AB and 596AC.

2.16 The note to subsection 596AA(1) provides two example scenarios where the Part may apply. These are:

- a company owner has removed assets from a company before it is wound-up, leaving outstanding unpaid employee entitlements; or
- a company group is structured in such a way that results in all the employee entitlement obligations being the debts of one entity in a corporate group which is wound up, while other entities of the group continue to exist.

[Part 1 of Schedule 1, item 4, note to subsection 596AA(1)]

2.17 These two example scenarios are not intended to limit the types of situations where the Part may apply. Other examples where the Part could potentially apply include circumstances where:

- there is avoidance of the payment of employee entitlements due to illegal phoenixing activity;
- a corporate group is restructured through inter-group asset and liability transfers, and one or more group entities transfer employees to a new trading entity which is created and added to the group. The entities from which employees are transferred retain certain employees, who are then made redundant. The transfer of assets and liabilities to other group entities leaves no capacity for the 'old' entities to pay the employee entitlements. The entities with the redundant employees are then put into administration and subsequently wound-up;
- a company director enters into a range of unviable and uncommercial transactions which strips a company of its liquid and marketable assets. The entity is then put into voluntary administration and is subsequently liquidated, exposing all the creditors to potential losses including the company's employees;
- a company officer intends to enter into a transaction that would avoid the payment of that company's employee entitlements, but ultimately the transaction fails to achieve the intended result and no entitlements are avoided; and
- company officers collude with select creditors of the company to transfer value out of the company, prior to the company being placed into voluntary administration and subsequently being wound-up. This behaviour results in the company being unable to meet its obligations to its other creditors, including its employees.

Persons who the Part might apply to

2.18 When the Part was introduced into the then *Corporations Act 1989* (Cth) in 2000, the amending Act (the *Corporations Law Amendment (Employee Entitlements) Act 2000* (Cth)) and its related explanatory memorandum, briefly outlined the persons to which the Part could apply.

2.19 These documents state the persons the Part could apply to include the company (with the outstanding employee entitlements) and the company's directors. No further guidance on the persons within scope of the Part was contained in those documents, other than a provision in the amending Act outlining the Part could still apply where the company with the employee entitlements was not involved in the relevant agreements or transactions.

2.20 As such, it was not made explicit what parties the Part may potentially apply to including third parties outside the relevant company.

2.21 To improve clarity about the persons potentially subject of the Part, the Part is intended to apply to the following persons, as a minimum:

- the company;
- that company's directors;
- that company's officers;
- other persons involved in the management of that company; and
- potentially a range of additional parties both internal and external to the company (for example, pre-insolvency advisors), depending on the facts of the relevant case.

2.22 As the Part is intended to apply to a very broad range of scenarios, the persons to whom the Part could potentially apply is also broad.

2.23 Additionally, Part 2.4 of the *Criminal Code Act 1995* (Cth) and section 79 of the *Corporations Act* can apply to capture and sanction the behaviour of persons involved in contraventions of the provisions of the Part.

An entitlement of an employee need not be owed to the employee

2.24 Subsection 596AA(2A) of the Bill specifies that employee entitlements need not be owed directly to an employee of a company to still be within scope of the protections provided by the Part. *[Part 1 of Schedule 1, item 6, subsection 596AA(2)]*

2.25 Subsection 596AA(2A) lists four example scenarios. These examples are not an exhaustive list of entitlements not owed to the employee but which are still protected by the Part.

2.26 Paragraph 596AA(2A)(a) outlines that an amount owed to an employee's dependants is an entitlement protected by the Part. This could for example include amounts an employee has compulsorily deducted from their salary to satisfy child support obligations, or payments made to the employee's dependants by the company as a result of injury compensation payable to the employee. *[Part 1 of Schedule 1, item 6, paragraph 596AA(2A)(a)]*

Example 1

Under the *Child Support (Registration and Collection) Act 1988* (Cth), Vegeta's employer, Destruction Pty Ltd, is obliged to collect amounts from Vegeta's salary and wages to meet his child support obligations for his son Trunks.

The child support amounts are deducted from Vegeta's net monthly salary, and are to be paid to the Department of Human Services by Destruction Pty Ltd, as the child support amount is a debt due to the Commonwealth.

Beerus, the owner of Destruction Pty Ltd, withholds the amounts from Vegeta's salary but does not pay those amounts to the Department of Human Services. Soon afterwards, Destruction Pty Ltd is placed into administration and then subsequently wound up.

Though the amounts of Vegeta's child support obligations are legally payable to the Department of Human Services by Destruction Pty Ltd, this does not prevent those unpaid amounts being employee entitlements protected by the Part.

2.27 Paragraph 596AA(2A)(b) further outlines that a superannuation contribution which should be payable to a superannuation fund by an employee's corporate employer, is an entitlement protected by the Part. Such contributions could include compulsory superannuation contributions payable by the corporate employer to a fund for the employee, or voluntary additional superannuation contributions of the employee deducted from their salary by the employer but not remitted to the fund. *[Part 1 of Schedule 1, item 6, paragraph 596AA(2A)(b)]*

2.28 Paragraphs 596AA(2A)(c) and (d) clarify that outstanding employee entitlements that are owed by the employer, and which are subsequently paid to employees by the Commonwealth (for example, under the Fair Entitlements Guarantee scheme) or paid by another party (for example, an employer representative body), will not impact the protections provided by the Part for those entitlements which remain unpaid by the company. *[Part 1 of Schedule 1, item 6, paragraphs 596AA(2A)(c) and (d)]*

2.29 Payments made directly to the employees by the Commonwealth or another entity for some or all of their outstanding employee entitlements, does not absolve relevant persons from the consequences of

possible contravention of the Part, or reduce the recovery options available by parties for payment of the entitlements that the company has not paid.

Example 2

Destruction Pty Ltd has 100 employees. Beerus, the owner of Destruction Pty Ltd, transfers all the assets of the company to another entity, and soon after retrenches all the employees.

The former employee's total unpaid employee entitlements (including redundancy payments) are \$5 million. The company does not have any funds to pay the outstanding amount, so the company is placed into voluntary administration and soon afterwards, enters into liquidation.

All the employees make applications under the Fair Entitlements Guarantee scheme for payment of certain outstanding entitlements. The scheme pays all these entitlements.

Even though the outstanding entitlements of the company are no longer payable in liquidation to the employees (as the employees have had their entitlements paid by the Commonwealth), this has no impact on the potential actions which parties such as the liquidator or the Commonwealth (exercising the rights of the employees) may take under the Part.

2.30 Finally, subsection 596AA(2) is amended to remove wording relating to employee entitlements not needing to be owed to employees, as that material has been consolidated in subsection 596AA(2A). [*Part 1 of Schedule 1, item 5, section 596AA(2)*]

Section 596AB: Entering into relevant agreements or transactions to avoid employee entitlements – offence provision

Subsection 596AB(1) – intention provision

2.31 Subsection 596AB(1) redrafts the Part's previous criminal offence provision to modernise and simplify it. The key amendments are:

- the criminal offence is no longer expressed in the negative (; and
- the physical and fault elements of the offence have been expressed in plain-english language so that it is easier to understand, which makes identifying the physical and fault elements in the offence simpler.

[Part 1 of Schedule 1, item 8 subsection 596AB(1)]

2.32 The redrafted criminal offence uses the same two limbs contained in its predecessor provision, which outline the specifics of the contravention. That is, it is a criminal offence for persons to enter a relevant agreement or transaction with the intention of:

- preventing the recovery of entitlements of employees of a company; or
- significantly reducing the amount of the entitlements of employees that can be recovered.

[Part 1 of Schedule 1, item 8, paragraphs 596AB(1)(a) & (b)]

2.33 The first limb is aimed at addressing circumstances where relevant agreements or transactions are entered into to avoid the payment of some or all of the entitlements of the employees of a company.

2.34 For example, a series of transactions may transfer the majority of the assets out of a company, after which the company enters voluntary administration and is subsequently wound-up. Transferring the assets out of the company which could have been used to help pay for the employee entitlements, is a way of preventing the payment of the entitlements. Such a series of transactions may be captured within the scope of the first limb.

2.35 The second limb is aimed at addressing circumstances where relevant agreements or transactions are entered into, which significantly reduce the amount of a company's employee entitlements which can be recovered.

2.36 For the purposes of section 596AB (and the Part more broadly), the term 'significant' is intended to have a meaning determined by the circumstances of the relevant agreements and transactions in each case.

2.37 Broadly however, a 'significant' reduction in the entitlements of employees:

- first, requires a material or substantial reduction in the amount of the entitlements that can be recovered;
- second, involves consideration of the quantum of the reduction as well as the proportionate size of the reduction produced; and
- third, can be determined solely based on the quantum of the reduction, in certain circumstances.

Example 3

Beerus, the owner of Destruction Pty Ltd, transfers \$1 million of assets to another entity. Soon afterwards, he retrenches all 100 of the company's employees, who are then owed \$5 million in employee entitlements.

The company is placed into voluntary administration and then enters into liquidation. The amount available to pay the outstanding entitlements is \$500,000.

The assets which were transferred may have been able to pay for an additional 20 per cent of the outstanding entitlements.

In the circumstances of the case, this transfer significantly reduces the entitlements that can be recovered. This is determined based on the relative percentage (being 20 per cent of the amount owed to the employees), as well as its quantum (which is \$1 million).

2.38 To contravene the criminal offence provision, a person must enter into relevant agreements or transactions with the intention of avoiding the payment of a company's employee entitlements, or of significantly reducing the amount of those entitlements that employees can recover.

2.39 Of note, contravention of the offence provision does not require such intention to be a dominant purpose. The person need not have a sole, primary, main or overriding intention of avoiding the payment of the company's employee entitlements or significantly reducing the amount of those entitlements.

2.40 Instead, it is sufficient to contravene the provision if the person has an intention:

- which includes the relevant intention;
- which is one of a number of other intentions; or
- where the intention to avoid or significantly reduce the entitlements is subsidiary to, or a minor part of, a different primary intention.

[Part 1 of Schedule 1, item 8, section 596AB(1)]

Example 4

Beerus, the owner of Destruction Pty Ltd, intends to transfer the assets of the company to a new entity as part of a scheme to avoid the payment of all liabilities to the company's creditors, by having the company put into voluntary administration and then wound up.

The company owes \$10 million to its creditors, as well as a total of \$1 million in outstanding employee entitlements, when all the company's employees are retrenched.

Though Beerus' dominant intention is to transfer assets to another entity to avoid Destruction Pty Ltd paying its liabilities to its creditors, Beerus has a subsidiary intention to avoid the payment of the company's employee entitlements.

Subsection 596AB(1A) – reckless as to the result provision

2.41 Subsection 596AB(1A) extends the fault element necessary to contravene the criminal offence provision in the Part to include a person who enters into a relevant agreement or transaction that avoids the payment of, or significantly reduces the amount of, the employee entitlements liabilities of a company where the person is 'reckless' as to those possible outcomes. *[Part 1 of Schedule 1, item 8, section 596AB(1A)]*

2.42 Subsection 596AB(1A) uses the same two limbs as are used in section 596AB(1), to outline the specifics of the contravention. These limbs are intended to be consistently defined with subsection 596AB(1) (see paragraph 2.32 above). Additionally, the term ‘significantly’ is defined in the same way as it is in subsection 596AB(1) (see paragraphs 2.36 and 2.37 above).

2.43 ‘Recklessness’ with respect to a result is defined in the schedule to the *Criminal Code Act 1995* (Cth) (in Division 5 ‘Fault elements’ at subdivision 5.4) as a person being aware of a substantial risk that a result will occur and having regard to the circumstances known to the person, it is unjustifiable to take that risk.

2.44 This definition notes that the question of whether taking a risk in the circumstances is unjustifiable, is one of fact.

2.45 Further, as recklessness is the fault element for the physical element in subsection 596AB(1A), proof of intention, knowledge or recklessness will satisfy that fault element. [*Part 1 of Schedule 1, item 8, note 2 to section 596AB(1A)*]

2.46 As such, in the context of subsection 596AB(1A), a person who enters a relevant agreement or transaction will be reckless if they are aware that there is a substantial risk that entering a relevant agreement or transaction is reasonably likely to avoid the payment of, or significantly reduce the recoverable amount of, the employee entitlements liabilities of the company, and doing so is unjustifiable in the circumstances.

Example 5

Whis, a company director of Destruction Pty Ltd, enters a transaction which transfers all the liquid assets of the company (valued at \$5 million) and some of its debts, to another company owned by Beerus, the owner of Destruction Pty Ltd.

Soon after, Destruction Pty Ltd is placed into voluntary administration and then wound up. All the employees are retrenched. The unpaid employee entitlements are \$3 million.

Before entering the transaction, Whis was aware that transferring the assets from the company would mean the company would be unable to pay its entitlements if the employees were made redundant. With regard to this substantial risk, Whis had no justification to take the risk.

In these circumstances, Whis is reckless as to the result, because the transaction is likely to prevent or significantly reduce the recovery of the employee entitlements.

Subsection 596AB(2) – application of the intent and recklessness provisions

2.47 Paragraph 596AB(2)(a) outlines that the intent and recklessness provisions (subsections 596AB(1) and (1A)) can apply even if the company which owes the employee entitlements to the employees, is not a party to the relevant agreement or transaction.

2.48 This provision ensures that the offence provisions operate as intended and have a broad application. If the company had to be a party to all relevant agreements and transactions that transgressed the offence provisions, this would unduly restrict the scope of the provisions. *[Part 1 of Schedule 1, item 8, paragraph 596AB(2)(a)]*

2.49 Paragraph 596AB(2)(b) outlines that the offence provisions will apply even where the relevant agreement or transaction has been approved by a court. This is because even if approved by a court, the agreements or transactions would have been entered into with the relevant intention or in circumstances where a person was reckless as to the possible results. *[Part 1 of Schedule 1, item 8, paragraph 596AB(2)(b)]*

2.50 Finally, both the intent and recklessness offence provisions can be contravened even where, despite the agreement or transaction, employee entitlements are not avoided, or significantly reduced, or have been recovered (in part or in full).

2.51 For example, a contravention of the criminal offence provision would still occur if a company director intentionally entered into a relevant agreement to deprive a company of all its liquid assets to pay its employee entitlements, but the relevant agreement subsequently failed to achieve this.

2.52 Paragraph 596AB(2)(c) is included to ensure that there is a strong deterrent in the law for those that attempt to avoid the payment of a company's employee entitlements or significantly reduce those entitlements that can be recovered, even if the attempt to achieve those aims is not ultimately successful. *[Part 1 of Schedule 1 - Amendments, item 8, paragraph 596AB(2)(c)]*

Example 6

Whis, a company director of Destruction Pty Ltd, intentionally enters a transaction to transfers all the liquid assets of the company (valued at \$5 million) to another company.

Completing the transaction will ensure that all the employee entitlements owed by Destruction Pty Ltd are able to be avoided.

However, the transaction fails. Even though the transaction failed and no employee entitlements were ultimately avoided, Whis contravenes subsection 596AB(1) by entering the transaction.

Subsection 596AB(2A) – deed of company arrangement

2.53 Subsection 596AB(2A) outlines that the intent and recklessness provisions (subsections 596AB(1) and (1A)) of the Part do not apply where relevant agreements or transactions are entered into by persons for the purposes of a deed of company arrangement (DOCA) executed by the company. *[Part 1 of Schedule 1, item 8, subsection 596AB(2A)]*

2.54 The purpose of excluding DOCAs from the operation of subsections 596AB(1) and (1A) of the Part is to avoid undermining the possible use of DOCAs in external administrations. Without this exemption, any executed DOCA that resulted in employee entitlements liabilities being reduced, could be at risk of contravening the criminal offence provisions of the Part.

2.55 The provisions on DOCAs in the Corporations Act (in Division 10 of Part 5.3A) already contain provisions to protect employee entitlements (being sections 444DA and 444DB). As such, the Part does not need to apply to those arrangements.

2.56 However, exclusion from the offence provisions of the Part will only apply where the company that has the outstanding employee entitlements executes the DOCA. The offence provisions could still apply to any DOCA executed by another company that produces the result of avoiding the payment of, or significantly reducing the amount of the employee entitlements that can be recovered, of the company that has the outstanding entitlements.

2.57 The note to subsection 596AB(2A) creates an offence specific defence, and states that a defendant will bear the evidential burden in relation to the subsection. *[Part 1 of Schedule 1, item 8, note to subsection 596AB(2A)]*

2.58 This is appropriate because potential defendants (being persons possibly contravening the criminal offence provision, such as the company and other persons employed by the company), would know whether relevant agreements and transactions were entered into for the purposes of a DOCA executed by the company, either because they are best placed to provide details of those relevant agreements and transactions, would be parties to the deed, or otherwise would have access to a copy of it.

Subsection 596AB(3) – reference to relevant agreements and transactions

2.59 Subsection 596AB(3) of the Part is amended by inserting a note to the end of the subsection to clarify what a relevant agreement may be. *[Part 1 of Schedule 1, item 9, note to section 596AB(3)]*

2.60 The subsection outlines that the terms ‘relevant agreement’ (outlined in section 9 of the Corporations Act) and transaction have extended definition, which can refer to a series or combinations of relevant agreements and/or transactions.

Increase in penalties for contravention of subsections 596AB(1) and 596AB(1A)

2.61 Schedule 3 of the Corporations Act is amended to specify that subsection 596AB(1A) is an offence provision. [*Part 1 of Schedule 1, item 18, Schedule 3 (table item 145)*]

2.62 Further and more importantly, the penalty for the criminal offence provisions in the Part is increased from:

- 1,000 penalty units or imprisonment for 10 years, or both;

to

- 4,500 penalty units or three time the benefit gained, or imprisonment for 10 years, or both (for individuals)
- 45,000 penalty units or three time the benefit gained or 10 per cent of the annual turnover of the entity (for corporations)

2.63 The enhanced penalties which have been introduced reinforce the seriousness of the offences in question, and the need for appropriate deterrence.

When do the criminal offence provisions apply?

2.64 The criminal offence provisions of the Part are intended to address contravention of those provisions at any time. This is to ensure that these provisions operate effectively to deter and sanction criminal behaviours of relevant persons.

2.65 The criminal offence provisions do not require the prevention of the recovery of entitlements of employees of a company, or the significant reduction of the amount of employee entitlements of a company that can be recovered, to have occurred. They only require that a person intended to produce those outcomes, or the person was reckless as to those results.

2.66 Practically though, it is likely that most prosecutions for contravention of the offence provisions would occur when a company enters into liquidation. This is because information about possible behaviours of persons which may contravene the Part would be accessible by the company’s liquidator, and reports on possible inappropriate behaviours within the company would be provided, by the liquidator and other parties, to ASIC for its investigation.

Section 596AC: Entering into relevant agreements or transactions to avoid employee entitlements – contravention and civil penalty

2.67 The Bill replaces the previous section 596AC with a new civil contraventions and civil penalties section. *[Part 1 of Schedule 1, items 10 and 11, section 596AC]*

Subsection 596AC(1) – contravention provision

2.68 Subsection 596AC(1) specifies that a person contravenes the provision if:

- they enter a relevant agreement or transaction; and
- the person knows, or a reasonable person in the position of the person would know, that the relevant agreement or transaction is likely to would
 - prevent the recovery of the entitlements of the employees; or
 - significantly reduce the amount of the entitlements that can be recovered; and
- after the relevant agreement or transaction is entered into, the company enters into liquidation.

2.69 Paragraph 596AC(1)(a) specifies the extended meaning of the terms relevant agreements and transactions (as used in subsection 596AB(3)) is to be used for section 596AC. *[Part 1 of Schedule 1, item 11, paragraph 596AC(1)]*

2.70 This definition is used to ensure that the criminal offence provisions of the Part and subsection 596AC(1) apply to the same agreements and transactions.

2.71 Paragraph 596AC(1)(b) then outlines the new objective test against which an assessment is made to determine if there has been a contravention of the subsection.

2.72 This objective test assesses whether the person knows, or a reasonable person in the specific circumstances of that person would have known or would be expected to have known, that the relevant agreements or transactions is likely to:

- prevent the recovery of the entitlements of the employees; or
- significantly reduce the amount of the entitlements that can be recovered.

[Part 1 of Schedule 1, item 11, paragraph 596AC(1)(b)]

2.73 For the purposes of the objective test, it is intended that the term ‘reasonable person’ uses its common law definition, which is an ordinary and unremarkable but reasonably educated and intelligent person.

2.74 Of note, paragraph 596AC(1)(b) uses the same two limbs used in sections 596AB(1) and 596AB(1A) to outline the specifics of the contravention. This construction is used in section 596AC to ensure:

- that the criminal offence provisions in the Part and section 596AC apply to the same types of behaviours. This means the criminal offence provisions plus the civil contravention and civil penalty provisions can operate together to deter relevant behaviours in a tiered way; and
- it will make it clear to the market the types of behaviours which are intended to be deterred or which will be sanctioned if they occur, as all the contravention provisions broadly apply to the same types of behaviours.

[Part 1 of Schedule 1, item 11, paragraph 596AC(1)]

2.75 Additionally, the term ‘significantly’ which is used in subparagraph 596AC(1)(b)(ii) is intended to take its meaning depending on the circumstances of the relevant case. However, the term is to be defined consistently for the purposes of relevant contravention provisions of the Part (refer paragraphs 2.36 and 2.37 above).

2.76 Paragraph 596AC(1)(c) specifies that subsection 596AC(1) is contravened only once a liquidator is appointed to the company. Thus action for contravention is only able to be brought once the company enters into liquidation (refer paragraphs 2.98 to 2.102). *[Part 1 of Schedule 1, item 11, paragraph 596AC(1)(c)]*

2.77 Finally, the note to section 596AC states that subsection 596AC(1) is a civil penalty provision. *[Part 1 of Schedule 1, item 11, note to section 596AC(1)]*

2.78 Civil penalty provisions within the Corporations Act allow courts to order individual defendants to pay penalties of up to \$200,000 where there has been a breach of a relevant civil provision. Once a court decides a breach of a civil penalty provision has occurred, ASIC can apply to the Court to seek disqualification orders of relevant persons from managing corporations for a period of time the court considers appropriate.

2.79 The introduction of the civil penalty provision into the Part will strengthen enforcement options available for contravention. Of note, this will mean that persons who engage in behaviours to avoid the payment of or significantly reduce the amount of employee entitlements that can be recovered, will be able to be disqualified and penalised for contravention of that subsection.

2.80 The table in subsection 1317E(1) is amended to list subsection 596AC(1) as a civil penalty provision. *[Part 1 of Schedule , item 17, subsection 1317E(1)]*

Subsection 596AC(2) – application of contravention provision

2.81 Subsection 596AC(2) outlines three specific circumstances where the contravention provision in subsection 596AC(1) will still apply. This subsection contains the same list of circumstances as subsection 596AB(2). This is a deliberate, to ensure the criminal offence provisions and section 596AC(1) have the same application. *[Part 1 of Schedule 1, item 11, section 596AC(2)]*

2.82 Paragraph 596AC(2)(a) outlines that the contravention provision will apply even if the company which owes the employee entitlements to the employees, is not a party to the relevant agreement or transaction.

2.83 This provision ensures that the contravention provision operates with a broad application. If the company had to be a party to all relevant agreements and transactions for the contravention provision to apply, this would undermine the impact of the provisions. *[Part 1 of Schedule , item 11, paragraph 596AB(2)(a)]*

2.84 Paragraph 596AC(2)(b) outlines that the contravention provision will apply even where the relevant agreement or transaction has been approved by a court. As such, the court’s approval will not create immunity from the breach of subsection 596AC(1) where the relevant agreement and transaction is likely to prevent the recovery of or significantly reduce the amount of employee entitlements that can be recovered. *[Part 1 of Schedule 1, item 11, paragraph 596AC(2)(b)]*

2.85 Finally, the contravention provision will still apply even where ultimately no employee entitlements are avoided by the relevant agreement or transaction.

2.86 For example, if a company director entered a contract which would transfer a large number of company assets (and as a result, the company could not pay its employee entitlements) but the agreement then failed, the contravention provision would still apply.

2.87 Paragraph 596AC(2)(c) ensures there is a deterrent for those who attempt to avoid the payment of a company’s employee entitlements or significantly reduce those entitlements that can be recovered, even if the attempt to achieve those aims is not successful. *[Part 1 of Schedule 1, item 11, paragraph 596AC(2)(c)]*

Subsection 596AC(3) – deed of company arrangement

2.88 Subsection 596AC(3) outlines that the contravention provision does not apply where relevant agreements or transactions are entered into

by persons for the purposes of a DOCA executed by the company. *[Part 1 of Schedule 1, item 11, subsection 596AC(3)]*

2.89 The purpose of this exemption is to ensure that the application of subsection 596AC(1) does not undermine the use of DOCAs in external administration.

2.90 The Corporations Act already contains provisions to protect employee entitlements in a DOCA (being sections 444DA and 444DB). As such, the Part does not need to apply to those arrangements.

2.91 The contravention provisions could still apply to any DOCA executed by another company that produces the result of avoiding the payment of, or significantly reducing the amount of the employee entitlements that can be recovered, of the company that owes the outstanding entitlements.

2.92 Of note, subsection 596AC(3) does not include the same requirement as subsection 596AB(2A) that a person relying on the exemption will bear a special evidential burden in relation to the subsection.

Subsection 596AC(4) – contravention by incurring a debt

2.93 It is possible that a relevant agreement or transaction in contravention of subsection 596AC(1) could also result in the company trading while insolvent, in contravention of section 588G.

2.94 To ensure that there is no double recovery for loss due to overlapping actions under the Corporations Act, a set of minor inserts and amendments are outlined in the Bill.

2.95 First, subsection 596AC(4) (which replicates the previous subsection 596AB(4)) outlines that if subsection 596AC(1) is contravened by a person incurring a debt for the purposes of section 588G, the debt which is incurred and the contravention are ‘linked’. *[Part 1 of Schedule 1, item 11, subsection 596AC(4)]*

2.96 Second, the definition of ‘linked’ which was originally set out in subsection 596AB(4), now repealed, is moved to the new subsection 596AC(4). *[Part 1 of Schedule 1, item 1, section 9 (definition of linked)]*

2.97 Third, paragraph 588N(b) is amended to prevent double recovery of the ‘linked’ amount if there was an action under section 596ACA (the new civil recovery provision of the Part) or there is an action under section 588M (the provision concerning the recovery of compensation for loss from insolvent trading). *[Part 1 of Schedule 1, item 2, section 588N(b)]*

When does the civil contravention and civil penalty provision apply?

2.98 It is the intention that the civil contravention and civil penalty will operate once a company enters into liquidation.

2.99 A consequence of this is a contravention of subsection 596AC(1) will not be able to be used to fund recovery action for unpaid employee entitlements while a company is operating.

2.100 When the Part was introduced in 2000, it was unclear in which circumstances the civil contravention provision could apply. Academic commentary on the Part suggested it could potentially apply at any time (while the company was operating, in voluntary administration, in liquidation or after the winding-up).

2.101 Since 2000, a number of new recovery options have been introduced for unpaid employee entitlements, where an employee's employer is not in liquidation. These include actions that can be taken against an employer under the *Fair Work Act 2009* (Cth) for statutory breach to pay wages and salary under for example, section 323 of that act.

2.102 Due to the availability of these alternative recovery options, it is not necessary for the contravention provision to operate in circumstances outside of liquidation.

Section 596ACA: Person who contravenes section 596AC liable to compensate for loss

2.103 The Bill repeals the previous section 596AC (the Part's previous civil recovery provision), and replaces it with a new recovery provision, section 596ACA. [*Part 1 of Schedule 1, item 11, section 596ACA*]

2.104 Unlike its predecessor section 596AC, the new civil recovery provision has been decoupled from the Part's criminal offence provision, so to reduce confusion about how the provision is intended to operate.

2.105 Under the civil recovery provision, compensation for loss or damage suffered by the employees of the company due to the impact of relevant agreements or transactions can be obtained where the persons who entered those agreements or transactions have contravened the objective test in section 596AC, and the company is being or has been wound-up. [*Part 1 of Schedule 1, item 11, subsection 596ACA(1)*]

2.106 Relevant persons may be liable to pay compensation, notwithstanding that ASIC has taken civil penalty proceedings against the persons for contravention of subsection 596AC(1) and a Court has made a declaration of contravention or pecuniary penalty orders under Part 9.4B of the Corporations Act. [*Part 1 of Schedule 1, item 11, paragraph 596ACA(2)(a)*]

Example 7

Beerus, the owner of Destruction Pty Ltd and Whis, a company director of that company, arrange a series of transactions which result in the accounts receivable ledger (valued at \$5 million) being sold in stages to a related entity for nominal consideration.

Soon after, Destruction Pty Ltd is placed into voluntary administration and then enters into liquidation. All 100 employees are retrenched. The unpaid employee entitlements when the company is wound-up is \$3 million.

The series of transactions entered into, when assessed using the objective test in subsection 596AC(1), clearly contravenes the provision.

ASIC initiates civil penalty proceedings against Beerus and Whis, with the Court making pecuniary penalty orders against them both for \$200,000.

Even though the Court has penalised both Beerus and Whis, this does not prevent relevant parties taking action under section 596ACA to seek compensation from Beerus and Whis for the \$3 million of unpaid employee entitlements.

2.107 Further, a person may still be liable to pay compensation notwithstanding that the person has been convicted of an offence against section 596AB. [*Part 1 of Schedule 1, item 11, paragraph 596ACA(2)(b)*]

Example 8

Beerus is convicted of entering a transaction with the intention of preventing the recovery of the entitlements of employees. He is penalised 1,000 penalty units (\$210,000).

Beerus's conviction does not prevent relevant parties taking action under section 596ACA to seek compensation from Beerus. Relevant parties will still need to prove Beerus contravened the objective test in subsection 596AC(1).

2.108 The company's liquidator is able to take action against relevant persons for compensation payable for contravention of subsection 596AC(1). Compensation in such cases will be payable to the company. The compensation that may be payable is the amount of the loss or damage which the employees of the company suffered because of the relevant agreement or transaction that was entered into by persons, or because of actions taken to give effect to the relevant agreement or transaction. [*Part 1 of Schedule 1, item 11, subsection 596ACA(3)*]

2.109 The maximum amount of loss or damage that could be recovered by a liquidator under a subsection 596AC(1) action will equal the total of the outstanding employee entitlements when the company enters winding-up. This will occur where relevant agreements or transactions are entered into by persons, or because of actions taken to give effect to those relevant agreements or transactions, which result in all

the employee entitlements of the company being avoided or not being paid.

2.110 Employees of the company are in certain circumstances, also able to take action against relevant persons for contravention of subsection 596AC(1). In such cases, the compensation payable for loss or damage they suffer, will be a debt due to the employee. *[Part 1 of Schedule 1, item 11, subsection 596ACA(4)]*

2.111 Any recoveries made by the employee will be deducted from amounts that the employee has proved in the liquidation of the company. *[Part 1 of Schedule 1, item 11, subsection 596ACA(5)]*

Example 9

Goku is an employee of Destruction Pty Ltd, who was retrenched when the company was wound-up. Goku believes Beerus, the company's owner, entered into a range of transactions to avoid the company's employee entitlement liabilities.

Goku complies with the formalities for bringing action under section 596ACA, after which he obtains judgment against Beerus for the full outstanding employee entitlement amount.

Goku's recovers his outstanding employee entitlements, which are paid to him. His proof of debt against the company (for his outstanding employee entitlements) is reduced to zero.

Sections 596AD and 596AE: minor amendments

2.112 Section 596AD, the current provision in the Part concerning double recovery, is amended to reflect the reforms made in the Bill to the Part's previous criminal offence and civil recovery provision. *[Part 1 of Schedule 1, item 12, section 596AD]*

2.113 Section 596AD is also amended to address issues of potential double recovery created by other amendments contained in the Bill. These relate to situations where

- a liquidator, an employee or another party recovers compensation in an action under section 596ACA, and this recovery is taken into account where a Court issues a civil penalty order under section 1317H of the Corporations Act as part of civil penalty proceedings for contravention of subsection 596AC(1); and
- a liquidator, an employee or another party recovers compensation in an action under section 596ACA, and this recovery is taken into account where a Court makes an employee entitlement contribution order under section 588ZA of the Corporations Act.

[Part 1 of Schedule 1, item 13, section 596AD]

2.114 The heading to the current section 596AE in the Corporations Act (the section concerning the effect of the Part's previous civil recovery provision), is amended to reflect the reforms to the Part's previous criminal offence and civil recovery provision. *[Part 1 of Schedule 1, item 14, section 596AE (heading)]*

2.115 Similarly, references to the previous section 596AC in the current section 596AE of the Corporations Act, are updated to reference section 596ACA. *[Part 1 of Schedule 1, item 15, section]*

Sections 596AF, 596AG and 596AH: Proceedings under section 596ACA

2.116 The following existing sections in the Part are repealed:

- Section 596AF – Employees may sue for compensation with the liquidator's consent;
- Section 596AG – Employee may give liquidator notice of intention to sue for compensation;
- Section 596AH – When employee may sue for compensation without liquidator's consent; and
- Section 596AI – Events preventing from suing

[Part 1 of Schedule 1, item 16, section 596AF - AI]

Section 596AF – Proceedings for compensation

2.117 The Part's previous provisions concerning employees taking civil recovery action (previous sections 596AF, 596AG and 596AH) have been consolidated into the new section 596AF.

Subsection 596AF(1) – Parties who can take civil recovery action

2.118 Subsection 596AF(1) specifies the parties (in addition to a company's liquidator) who can bring civil recovery action under section 596ACA, and the conditions which they must comply with to take such action.

2.119 The relevant parties who can bring a recovery action for loss or damage under section 596ACA are:

- the Commissioner of Taxation;
- the Fair Work Ombudsman;
- the Secretary of the Department administering the *Fair Entitlements Guarantee Act 2012* (Cth) (currently the Department of Jobs and Small Business); and
- employees of the company.

[Part 1 of Schedule 1, item 16, subsection 596AF(1)]

2.120 Under previous sections 596AF, 596AG, and 596AH, employees had the ability to take recovery action either with the liquidators consent, or with the approval of the Court. However this civil recovery action has not been used by any employee since the relevant provisions were introduced into the law in 2000.

2.121 Noting this, the purpose of expanding the parties who can bring a civil recovery action under section 596ACA to include three government bodies, is to enhance the deterrent effect, and recovery potential, of the Part.

2.122 Having a wider range of parties with an ability to take action will encourage greater usage of the Part's civil recovery provision, which is expected to lead to enhanced recoveries of employee entitlements.

2.123 Of note:

- employees who take civil recovery proceedings under section 596ACA will take action to recover only their own loss or damage;

but

- the three government bodies who take civil recovery proceedings under section 596ACA will take action to recover all the loss or damage for all the employees of the company.

2.124 The government bodies taking civil recovery action are thus taking an action equivalent to that which the company's liquidator can take.

Subsections 596AF(2) and 596AF(3) – Liquidator or Court consent to proceed

2.125 Subsection 596AF(2) outlines that where a liquidator has been appointed to a company, any parties wishing to take civil recovery action need to obtain the liquidator's written consent to proceed, or obtain the approval of the Court. *[Part 1 of Schedule 1, item 16, subsection 596AF(2)]*

2.126 A liquidator has 30 days to respond in writing to a written request from any of the parties to take civil recovery action under section 596ACA. They can either provide their consent to any of the parties to proceed, refuse the request of the party, or not respond within the 30 day period. *[Part 1 of Schedule 1, item 16, paragraphs 596AF(3)(a) & (b)]*

2.127 A court can grant leave to a party to take civil recovery action under section 596ACA where the liquidator has refused a request or not responded to a request, where it is satisfied it is appropriate to give that leave. *[Part 1 of Schedule 1, item 16, paragraph 596AF(3)(c)]*

2.128 In coming to that decision, the Court must have regard to whether the liquidator or another person will begin proceedings under section 596ACA, and any other matters the court considers relevant. *[Part 1 of Schedule 1, item 16, subparagraphs 596AF(3)(c)(i) & (ii)]*

Section 596AG – Events preventing proceedings under section 596ACA

2.129 Section 596AG lists a range of events that prevent government bodies and employees taking civil recovery action under section 596ACA.

2.130 Subsection 596AG(1) lists four events which prevent employees and government officials taking civil recovery action under section 596ACA. They are where the company liquidator:

- is taking civil recovery action under section 596ACA to recover for the loss or damage for all the employees of the company;
- is seeking a court order that a transaction was a voidable transaction under section 588FF, and this same transaction also contravened subsection 596AC(1) or was part of the a contravention of that subsection;
- has begun proceedings under section 588M for recovery of compensation for loss due to insolvent trading, where the relevant transaction also contravenes the Part; or
- has intervened in an application for a civil penalty order under section 588G in relation to insolvent trading.

[Part 1 of Schedule 1, item 16, subsection 596AG(1)]

2.131 The four events listed essentially prevent employees and government officials taking action because the liquidator is already taking action in relation to the same contravention.

2.132 The list of four events in subsection 596AG(1) are taken from the Part's previous section 596AI.

2.133 Additionally, subsection 596AG(2) specifies that an employee cannot bring a civil recovery action where one of the government bodies has begun taking action. The employee is prevented from taking such action because the government bodies would already be taking action on behalf of that employee and all the other employees to recover all of their loss and damage. *[Part 1 of Schedule 1, item 16, subsection 596AG(2)]*

Section 596AH – Joining parties to proceedings

2.134 Section 596AH outlines that the employees of the company, any of the government bodies which can take civil recovery action under section 596ACA, and the liquidator, can apply to the Court to be joined as parties to proceedings under section 596ACA.

2.135 Subsection 596AH(1) allows the three government bodies and any of the employees of the company, to apply to the Court to be joined as a party to the liquidator’s proceedings under section 596ACA. Such parties can seek to join the proceedings, as they are interested parties to the action that is underway. *[Part 1 of Schedule 1, item 16, subsection 596AH(1) of the Corporations Act 2001]*

2.136 Subsection 596AH(2) concerns civil recovery proceedings which have been initiated by one of the government bodies which can take civil recovery action under section 596ACA. Subsection 596AH(2) allows any other government body, an employee of the company to which the proceedings relate, and the company’s liquidator, to apply to the Court to be joined to the proceedings. Such parties can seek to join the proceedings, as they are interested parties to the action that is underway. *[Part 1 of Schedule 1, item 16, subsection 596AH(2) of the Corporations Act 2001]*

Consequential amendments

2.137 There are no consequential amendments.

Application and transitional provisions

2.138 The provisions will apply in relation to a relevant agreement or a transaction that is entered into on or after the commencement of the Bill which will be the day after the Bill receives Royal Assent. *[Part 4 of Schedule 1, item 31, section 1647]*

Chapter 3

Contribution orders

Outline of chapter

3.1 Part 2 of Schedule 1 to the Bill inserts new provisions into Part 5.7B of the Corporations Act that allow contributions to be sought from entities in a corporate group, for the payment of outstanding employee entitlements of an insolvent member of that corporate group, in certain limited circumstances.

Context of amendments

3.1 Many businesses operate using a group structure of several companies, with a parent company controlling the group, and each company in the group being a separate legal entity with limited liability. Such groups are often referred to as 'company groups' or 'corporate groups'.

3.2 Corporate groups can structure themselves in a multitude of ways. Amongst those options, a group can legitimately be structured so that one or more companies in the group hold employees and associated liabilities, while other companies in the group hold the assets of the group.

3.3 Where corporate groups adopt such structures and legally operate as a single economic unit (for example, by all the entities in the group entering a deed of cross guarantee for all the group's liabilities), the insolvency of the corporate group members with employee entitlement liabilities are not likely to adversely impact payment of those entitlements. This is because the legal guarantee would require all the solvent group members to meet the insolvent member's debts.

3.4 Where corporate groups adopt such structures without entering a deed of cross guarantee or similar arrangement, but, in reality, operate like a single economic entity (or in a similar highly integrated way), the insolvency of a corporate group member with employee entitlement liabilities can result in those entitlements not being paid. As the insolvent entity often has no or limited assets to meet those entitlements, it won't be able to pay the entitlements. Where there is no ability to make the other entities of the corporate group pay or otherwise contribute to the insolvent employing entity's liabilities (due to each group member being a separate legal entity), they are most unlikely to pay the outstanding amounts either.

3.5 This can be the case even where certain entities in that corporate group have obtained economic benefits from the now insolvent group member's employees' work, but were not being charged the full arm's-length costs for that labour.

3.6 Insolvency of such entities can have the consequence of shifting the cost of the corporate group's outstanding employee entitlement obligations to the FEG scheme, even where the corporate group as an economic entity has capacity to pay the outstanding entitlements, but chooses not to as it is not legally obliged to.

3.7 The use of corporate group structures in such ways allows the corporate group to avoid responsibility for paying its outstanding employee entitlements, and leaves the FEG scheme vulnerable to exploitation. That is, the corporate group is able to shift the costs of the outstanding employee entitlements to the FEG scheme, with the taxpayer effectively subsidising the corporate group to pay its former employees for outstanding costs that the group has not fully paid for.

3.8 In such circumstances, current actions available to liquidators of an insolvent group entity to recover amounts from other corporate group members are not effective to tackle this issue.

Example 10

Beerus is the owner of Mass Destruction Group which has three entities: Destruction Pty Ltd (the trading entity), Reconstruction Pty Ltd (the asset owning entity) and Destruction Personnel Pty Ltd (the employing entity). The employees of Destruction Personnel Pty Ltd manufacture widgets for sale by other entities in the Group. In this sense Destruction Personnel has been established for the dominant purpose of servicing the trading and asset owning entities.

Whis is the director of Destruction Personnel Pty Ltd and reports to Beerus that the factory is facing hard times. It needs to restructure to gain efficiencies which will involve shedding staff and investing in new equipment. Beerus forms the view that the Destruction Personnel operating model is too outdated to continue, so he will close it down and seek production services elsewhere. As a result, all 100 employees of Destruction Personnel are retrenched, being owed \$3 million in employee entitlements.

As Destruction Personnel has no assets to fund the employee entitlements, it enter into administration and then winding up. While the remaining two entities in Mass Destruction Group have sufficient financial capacity to pay the employee entitlements of Destruction Personnel, there is no deed of cross guarantee in place and they choose not to do so. The unpaid entitlements of retrenched employees of Destruction Personnel Pty Ltd are paid under the FEG. Destruction Pty Ltd and Reconstruction Pty Ltd continue to operate successfully under the new production supply model.

3.9 New provisions are being introduced in the Corporations Act to address these circumstances. The new provisions are similar to those

existing in *New Zealand's Companies Act 1993* (NZ). These provisions allow contributions to be sought from entities across a corporate group for the payment of outstanding employee entitlements of insolvent group entities, in appropriate circumstances.

Summary of new law

3.10 Part 2 of Schedule 1 to the Bill introduces reforms to the insolvency provisions of the Corporations Act that will allow recovery of unpaid employee entitlements of insolvent corporate group members from members of their corporate group, in certain circumstances.

3.11 In summary:

- liquidators (plus the ATO, FWO, and DJSB) will be able to seek 'employee entitlements contribution orders' that require entities within a group of entities (including a corporate group) to contribute in certain circumstances to the payment or recovery of employee entitlement debts of an insolvent group entity where:
 - it is 'just and equitable'; and
 - the group entities have benefitted from the labour of the employees of the insolvent entity on other than arms-length terms;
- the scope of the 'employee entitlements contribution order' is limited to entitlements of employees within the meaning of the range of entitlements protected under Part 5.8A;
- the existence and composition of a 'corporate group' or 'group of entities' subject to the 'employee entitlements contribution order' will be determined by a court when a contribution order application is made;
- whether making the contribution order is 'just and equitable' will be determined by a court when a contribution order is made; and
- the full 'non-arm's-length benefit' will be determined by a court when a contribution order application is made.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Liquidators can apply to the Court to	No equivalent.

<p>seek an ‘employee entitlements contribution order’ from entities across a corporate group to pay the employee entitlement debts (including unpaid superannuation and redundancy payouts) of an insolvent entity of that entity group where:</p> <ul style="list-style-type: none"> - it is just and equitable; and - the other group entities have benefitted from the labour of the employees of the insolvent entity on other than arm’s-length terms. 	
<p>The ATO, FWO and DJSB will be able to apply to the Court to seek ‘employee entitlements contribution orders’ from entities across a corporate group, in certain limited circumstances.</p>	<p>No equivalent.</p>
<p>For the purposes of making an ‘employee entitlements contribution order’, the Court will have significant flexibility under the new provisions to determine</p> <ul style="list-style-type: none"> - who the relevant members of a contribution order group are - who the contributing entities are - the amount that would be reasonable for contributing entities to pay towards the unpaid employee entitlements; and - whether it is ‘just and equitable’ to make the order. 	<p>No equivalent.</p>
<p>The Court will have the ability to make any other orders and give any directions appropriate to give effect to the ‘employee entitlements contribution order’.</p>	<p>No equivalent.</p>

Detailed explanation of new law

3.12 Part 2 of Schedule 1 to the Bill makes amendments to the Corporations Act to insert new provisions which will allow the Court to

make 'employee entitlements contribution orders' that require entities within an entity group (a corporate group or otherwise) to contribute in certain circumstances to the payment or recovery of employee entitlement debts of an insolvent group entity where:

- it is 'just and equitable'; and
- the group entities have benefitted from the labour of the employees of the insolvent entity on other than arms-length terms.

Section 588ZA: Employee entitlements contribution orders

3.13 The Bill introduces a new division (Division 8 – Employee entitlements contribution orders) into the Corporations Act at the end of Part 5.7B.

3.14 As part of the new division, new section 588ZA outlines that:

- a Court may make an employee entitlement contribution order where a liquidator, the ATO, the FWO or the DJSB makes an application for such an order.
- the employee entitlements contribution order can apply to entities across an entity group to ensure they pay contributions towards the employee entitlement debts (including unpaid superannuation and redundancy payouts) of an insolvent entity of that corporate group where:
 - it is just and equitable; and
 - the other group entities have benefitted from the labour of the employees of the insolvent entity on other than arm's length terms.
- for the purposes of making an 'employee entitlements contribution order', a Court will have significant flexibility to determine:
 - who the relevant members of a contribution order group are;
 - who the contributing entities will be;
 - the amount that would be reasonable for contributing entities to pay towards the unpaid employee entitlements; and
 - whether it is 'just and equitable' to make the order.
- the Court will have the ability to make any other orders and give any directions appropriate to give effect to the 'employee entitlements contribution order'.

[Part 2 of Schedule 1, item 19, section 588ZA]

Making an employee entitlements contribution order

3.15 Under section 588ZA, a Court can make an order (an 'employee entitlements contribution order') that certain entities within a 'contribution order group' contribute in certain circumstances to the payment or recovery of the employee entitlement debts of an insolvent group entity.

[Part 2 of Schedule 1, item 19, subsections 588ZA(1) & (2)]

- Section 588ZA uses the word 'entity' rather than 'corporations' in certain provisions. This is because those provisions are referring to entities defined in section 64A of the Corporations Act.

3.16 To make such an order, a court has to receive an application from:

- the liquidator of the insolvent group entity company
- the ATO
- the FWO; or
- the Secretary of the Department administering the *Fair Entitlements Guarantee Act 2012* (Cth) (currently the Department of Jobs and Small Business).

[Part 2 of Schedule 1, item 19, subsection 588ZA(5)]

3.17 To encourage applications being made to Court in appropriate cases, any of the parties which have standing under subsection 588ZA(5) can make an application, once the necessary information the Court requires is available (see paragraphs 3.26 below).

3.18 It would be expected that in the majority of cases, the insolvent group entity's liquidator would be the party making the application for the order.

3.19 To allow for circumstances where a company liquidator may not be adequately funded, the liquidator may not wish to take the risk of bringing the action, and to address circumstances where the liquidator could be conflicted, the three listed government bodies will be able to make applications as and when appropriate.

3.20 For a Court to make an order, the Court needs to be satisfied of the five things specified in subsections 588ZA(1)(a) to (e).

First requirement – a company is being wound-up

3.21 The first requirement is the Court must be satisfied that a company (the 'insolvent company') has entered liquidation. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(1)(a)]*

3.22 The parties with standing to make an application for the order should not have difficulty proving this to the Court's satisfaction. This is because the applicants will be either the insolvent company's liquidator, or government bodies who would be aware the entity is insolvent because of reasons including that:

- payments to redundant employees have been made under the FEG scheme by DJSB;
- the ATO has proved for debts in the insolvency; or
- the FWO and the ATO have been pursuing various actions against that entity, and those actions ceased once the entity was wound-up.

Second requirement – outstanding employee entitlements

3.23 The second requirement is the Court must be satisfied the insolvent company has unpaid employee entitlements of the type specified in subsection 596AA(2) of the Corporations Act (being the entitlements protected by the Part). *[Part 2 of Schedule 1, item 19, paragraph 588ZA(1)(b)]*

3.24 The employee entitlements that can be the subject of a contribution order are the same entitlements that would receive preferential payment in a winding-up, as outlined in section 556 of the Corporations Act. This is a deliberate design feature of the contribution order.

3.25 With this requirement, a Court will be able to be satisfied of the unpaid employee entitlements in question, once the company's liquidator has determined this amount through the process for proof of debts owed by the company. Until this process is finished and the quantum of the outstanding entitlements is determined, an application for an order will not be able to be progressed.

Third requirement – contributing entities and contribution order group

3.26 The third requirement is the Court must be satisfied that the 'contributing entity' is a member of the same 'contribution order group' as the insolvent company. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(1)(c)]*

3.27 Under section 588ZA, a Court can make an order that a contributing entity pay the liquidator of the insolvent entity an amount in relation to the unpaid employee entitlements of that entity.

3.28 The only entities that can be 'contributing entities' to the payment of the insolvent entity's unpaid employee entitlements, are those entities which are 'members of the same contribution order group' as the insolvent entity. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(1)(c) and subsection 588ZA(4)]*

3.29 Subsection 588ZA(4) lists six tests which a Court can use to determine the composition of a contribution order group. *[Part 2 of Schedule 1, item 19, paragraphs 588ZA(4)(a) to (f) of the Corporations Act 2001]*

3.30 The first five tests (outlined in paragraphs 588ZA(4)(a) to (e)) use a number of standard corporate entity relationship tests to determine if the insolvent corporation and another corporation or entity are related, and thus part of the same corporate group or group of entities.

3.31 These tests are:

- an entity is currently or was in the past, a related body corporate (according to the definition in section 50 of the Corporations Act) to the insolvent entity; or
- an entity is currently or was in the past, a related body corporate to another entity that is a related body corporate (according to the definition in section 50 of the Corporations Act) to the insolvent entity; or
- an entity is controlled or was previously controlled (as outlined in section 50AA of the Corporation Act), by a related body corporate of the insolvent entity; or
- an entity that represents to the public that it is related to the insolvent entity; or
- both entities are part of the same consolidated entity; or
- both entities are part of a collection of entities that functions as a single economic group

3.32 The Court can use the above tests to map out the relevant corporate group or group of entities that the insolvent corporate entity was a part of.

3.33 Courts can apply any tests in combination that are considered relevant to determine the relationships between entities and the make-up of the contribution order group.

3.34 The application of the tests allows former corporate group entities or other entities to be included in the ‘contribution order group’, if this is appropriate.

3.35 With the test outlined in paragraph 588ZA(4)(d) (the entities represent to the public that it is related to the other entity), the court may consider material such as:

- promotional material published by relevant entities;
- information in documents lodged with ASIC or other Government entities;

- information in loan guarantee documents;
- annual reports of relevant entities; and
- details of entities parties to relevant deeds of cross guarantee.

3.36 With the test outlined in paragraph 588ZA(4)(e) (both entities are part of the same consolidated entity), the court may consider material such as:

- consolidated accounts prepared according to relevant accounting standards;
- documents lodged with ASIC related to the relevant consolidate entity; and
- materials provided to financial institutions for purposes of financing for the consolidated entity.

3.37 With the sixth test outlined in paragraphs 588ZA(4)(f) (both entities are part of a collection of entities that functions as a single economic group), Courts may consider examining the legal structure of a set of entities, and then making a determination of how those entities operate on a day to day basis.

3.38 For entities to comprise a single economic group, they need to operate closely together to achieve a set of common aims. The more integrated the operation of the entities, the more likely they will be operating as a single entity. For example, if each of the entities in the group supports each other to achieve a common aim, and the employees of the different entities work together on common tasks, it is more likely the entities will be a single economic entity.

3.39 Conversely, a group of entities that operate relatively independently and are not intertwined in their operations, are less likely to comprise a single economic group.

Fourth requirement – benefit directly or indirectly from the work done by employees of the insolvent entity

3.40 The fourth requirement is the Court must be satisfied that a ‘contributing entity’ has benefitted, directly or indirectly, from work done by those employees of the insolvent entity with the unpaid entitlements. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(1)(d)]*

3.41 For the purposes of this requirement, the Court may examine the entities which make up the ‘members of the same contribution order group’ and determine whether any of these entities should be ‘contributing entities’.

3.42 To determine whether an entity should be a ‘contributing entity’, an assessment of each ‘member of the same contribution order group’ may be made by the Court to determine whether each entity received a

benefit, directly or indirectly, from the work done by the employees of the insolvent company.

3.43 The court will make a determination whether each entity received a benefit from the labour of the employees of the insolvent entity on other than arms-length terms.

3.44 The number of contributing entities in any case will depend on the specific circumstances. It is possible that every ‘member of the same contribution order group’ could be a ‘contributing entity’.

3.45 To assist the Court in making this assessment, the following are a range of factors that may be considered:

- the rate that the insolvent group member charged other members of the corporate group or entity group, and the difference between that and the full market rate for the services provided;
- which group entities the employees of the insolvent entity undertook work for;
- which group entities made payments for the use of the insolvent company’s employees’ labour;
- whether there were any group entities which did not pay for benefits they received, or if group members paid for the benefits other group members received;
- whether the wages, salaries and other benefits of the employees of the insolvent group member were the same or similar to employees of other corporate group members (as this may assist to determine the full market rate);
- the total outstanding amount of the unpaid employee entitlements of the insolvent corporate group member (which is the potential maximum value of benefits received but not paid for by the contributing entities); and
- any other information the court thinks is relevant in each case.

Fifth requirement – it is just and equitable to make the order

3.46 The fifth requirement is the Court must be satisfied that it is just and equitable to make the order in the particular case. [*Part 2 of Schedule 1, item 19, paragraph 588ZA(1)(e)*]

3.47 Essentially the court is making a decision that it is appropriate in the circumstances that other members of the relevant entity group contribute to pay the outstanding employee entitlements of the insolvent entity, because:

- the other entities did not pay the appropriate rate for the benefits they received; and
- this shortfall in the payment contributed to the employees of the insolvent entity having unpaid employee entitlements because insufficient funds were provided to pay these entitlements, including their redundancy.

3.48 To assist the Court in making a determination that it is just and equitable to make an order, the following is a list of factors that may be considered:

- the extent to which entities of the corporate group obtained economic benefits from the labour of the insolvent entity on non arm's-length terms (that is, whether the insolvent entity had charged a full market rate to the other group entities for the use of the employees' services or another rate);
- the control and management relationship between entities in the group, and whether the insolvent entity had common directors and officers with the related group entities;
- whether assets had been transferred from the now insolvent entity to other entities which could have satisfied the unpaid entitlements;
- efforts that the entities of the group and their directors made to provision for the full impact of the employee redundancies;
- efforts that the directors and officers of the insolvent company made to ensure the payment of the outstanding employee entitlements;
- any efforts made by corporate group entities to delay, retard, avoid or circumvent the effect of a potential contribution order, such as transferring assets from entities which received the benefit of non-arm's length labour;
- the impact on the other group entities of making the payments ordered, such as any impact on their solvency or ability to make distributions to creditors in insolvency;
- which group entities the employees believed was their employer;
- whether all the employee entitlement payments and other obligations (including payment of employees' superannuation, their income taxation withholding amounts, and other payments) had been met in the past, and whether payments were on time; and

- any other matters the court thinks fit in each case.

Court orders made to contributing entities

3.49 The Court may order the contributing entity to make a payment to the liquidator of the insolvent company that reflects the benefit obtained by that entity. This benefit is calculated as the difference between what was paid, directly or indirectly, for the benefit received and what the Court believes would be reasonable in the circumstances if the insolvent entity and the contributing entity operated as if they were dealing at arm's-length terms. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(2)(a)]*

3.50 The contributions that the Court orders 'contributing entities' to make cannot collectively total more than the unpaid employee entitlements of the insolvent entity. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(2)(b)]*

Enforcement of contribution orders by the Court

3.51 The Court may make any other orders and give any directions that the Court believes are necessary to give effect to an employee entitlements contribution order, and to ensure it is paid to the insolvent company's liquidator. *[Part 2 of Schedule 1, item 19, paragraph 588ZA(2)(b)]*

Consequential amendments

3.52 There are no consequential amendments.

Application and transitional provisions

3.53 The provisions will apply from the day after Royal Assent, and will apply in relation to the wind-up of a company (the insolvent company) that begins on or after commencement of the provisions. *[Part 4 of Schedule 1, item 31, section 1648]*

Chapter 4

Disqualification from managing corporations

Outline of chapter

4.1 Part 3 of Schedule 1 of the Bill amends Part 2D.6 of the Corporations Act to introduce new provisions to disqualify company directors and company officers with a track record of involvement in insolvencies where government employee entitlements schemes fund unpaid employee entitlements.

Context of amendments

4.1 Under the Corporations Act, company directors and officers can be disqualified from managing corporations in certain circumstances that are outlined in Part 2D.6. Disqualification of persons can occur automatically, by application to a court to order disqualification of a person, or by a determination of ASIC.

4.2 The existing disqualification provisions in Part 2D.6 do not specifically mitigate behaviours that impact the FEG scheme, in particular where company directors and officers manage companies where there is reliance on FEG on multiple occasions to effectively subsidise the cost of running their business.

4.3 The amendments to Part 2D.6 in the Bill introduce new disqualification provisions that better target those company directors and officers whose behaviours are impacting the FEG scheme.

Summary of new law

4.4 Part 2D.6 of the Corporations Act is amended to introduce new provisions to disqualify company directors who have a track record of involvement in insolvencies where government employee entitlements schemes have funded employee entitlements.

4.5 In summary, ASIC and the Courts may disqualify persons from managing corporations where companies to which they have been appointed have been liquidated, and the former employees of those companies relied on a government employee entitlements scheme to pay their outstanding employee entitlements.

- This may occur where, within 10 years, there were two or more separate occasions where:
 - there was a breach by the company or the director or the officer of the Corporations Act; and
 - FEG did not receive any return or only a minimal return, through the liquidation process or other recovery processes.
- ASIC will be able to disqualify company directors and officers under the new provisions for a period of up to 10 years. The Court will be able to disqualify directors and officers for a period the Court thinks is appropriate.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>ASIC and the Courts may disqualify persons from managing corporations where companies to which they have been appointed have been liquidated, and the former employees of those companies relied on a government employee entitlements scheme to pay their outstanding employee entitlements.</p> <p>This may occur where, within a 10 year period, and on two or more separate occasions, the company was liquidated, and on each occasion:</p> <ul style="list-style-type: none"> - there was a breach by the company or the director or the officer of the Corporations Act; and - FEG did not receive any return or only a minimal return, through the liquidation process or other recovery processes. <p>ASIC will be able to disqualify persons under the new provisions for a period of up to 10 years.</p> <p>The Court will be able to disqualify persons under the new provisions for a period the Court thinks appropriate.</p>	<p>No equivalent.</p>

Detailed explanation of new law

4.6 Part 2D.6 is amended to introduce two new disqualification provisions to mitigate the impact of behaviours of certain company directors and officers on the FEG scheme. The new provisions will operate where multiple entities have failed and there was reliance on FEG for the payment of employee entitlements to the redundant workers of those entities, which effectively subsidised the cost of running the businesses.

Section 206EAB: Court power of disqualification

4.7 Section 206EAB allows a Court, on application of ASIC, to disqualify a person from managing corporations for a period of time that the Court considers appropriate, where the Court is satisfied the disqualification is justified. *[Part 3 of Schedule 1, item 25, subsection 206EAB(1)]*

4.8 The Court can disqualify persons under section 206EAB where companies to which persons have been appointed were involved in breaches of the Corporations Act and had former employees who relied on the FEG scheme for the payment of their outstanding employee entitlements, and this occurred on two or more occasions within 10 years, and;

- on each occasion, there was a breach by the company or the company director or the officer of the Corporations Act; and
- the FEG scheme did not receive a return through the liquidation process, or only received a minimal return of 10 per cent or less.

[Part 3 of Schedule 1, item 25, subsections 206EAB(1), (2) & (3)]

4.9 The persons who may be subject to disqualification by the Court include persons who are officers of the corporation and persons who ceased being officers of the corporation in the last 12 months, where redundant employees of that corporation were paid their entitlements by the FEG scheme. *[Part 3 of Schedule 1, item 25, subsections 206EAB(1), (2) & (3)]*

4.10 To be disqualified by the Court, relevant persons must have contravened the requirements of the Corporations Act or the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) in relation to each corporation. Alternatively, at least two of the corporations which they were an officer of, must have contravened either of those Acts while they were an officer. *[Part 3 of Schedule 1, item 25, paragraph 206EAB(2)(d)]*

4.11 No connection is required between the contraventions of the company director, company officer or the company mentioned in paragraph 206EAB(2)(d), the advance of employee entitlements under the FEG scheme and any unrecovered FEG advances in the company's

liquidation process. Any contravention of the Corporations Act is sufficient to satisfy the requirements of section 206EAB.

Section 206GAA: ASIC's power of disqualification

4.12 Section 206GAA allows ASIC to disqualify a person from managing corporations for up to 10 years where ASIC is satisfied the disqualification is justified. *[Part 3 of Schedule 1, item 27, subsection 206GAA(1)]*

4.13 ASIC can disqualify under section 206GAA where companies to which persons have been appointed were involved in breaches of the Corporations Act and had former employees who relied on the FEG scheme for the payment of their outstanding employee entitlements, and this occurred on two or more occasions within 10 years, and;

- on each occasion, there was a breach by the company or the company director or the officer of the Corporations Act; and
- the FEG scheme did not receive a return through the liquidation process, or only received a minimal return of 10 per cent or less.

[Part 3 of Schedule 1, item 27, subsections 206GAA(1), (2) & (3)]

4.14 ASIC must provide the person with a notice outlining that ASIC intends to disqualify them from managing corporations for contravention of the requirements of section 206GAA, and provide them with an opportunity to be heard. *[Part 3 of Schedule 1, item 27, paragraph 206GAA(1)(b)]*

4.15 The persons who may be subject to disqualification by ASIC includes person who are officers of the corporation and persons who ceased being officers of the corporation in the last 12 months, where redundant employees of that corporation were paid their entitlements by the FEG scheme. *[Part 3 of Schedule 1, item 27, paragraphs 206GAA(2)(a) & (b)]*

4.16 To be disqualified by ASIC, relevant persons must have contravened the requirements of the Corporations Act or the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) in relation to each corporation. Alternatively, at least two of the corporations which they were an officer of, must have contravened either of those Acts while they were an officer. *[Part 3 of Schedule 1, item 27, paragraph 206GAA(2)(d)]*

4.17 No connection is required between the contraventions of the company director, company officer or the company mentioned in paragraph 206GAA(2)(d), the advance of employee entitlements under the FEG scheme and any unrecovered FEG advances in the company's liquidation process. Any contravention of the Corporations Act is sufficient to satisfy the requirements of section 206GAA.

4.18 In making a determination that the disqualification of the person is justified, ASIC may have regard to:

- the person's conduct in relation to the management, business or property of any corporation (and not just the corporations which are the subject of the disqualification);
- whether the disqualification would be in the public interest (for example, prevent the person from managing further corporations which are likely to be wound-up and then impose cost on the taxpayer via claims on the FEG scheme); and
- any other matter that ASIC considers is appropriate in the circumstances.

[Part 3 of Schedule 1, item 27, subsection 206GAA(4)]

4.19 When ASIC disqualifies a person under section 206GAA, they must serve the person with a notice that advises them they have been disqualified. This notice will amongst other things, specify the time period that the person is disqualified for. *[Part 3 of Schedule 1, item 27, subsection 206GAA(6)]*

4.20 A person dissatisfied with ASIC's decision, can seek that ASIC reviews the disqualification or can pursue their rights to have the decision reviewed by the Administrative Appeals Tribunal.

4.21 The disqualification takes effect from the time the notice is served on the person. *[Part 3 of Schedule 1, item 27, subsection 206GAA(7)]*

Section 206GAB: ASIC's power to grant leave

4.22 Section 206GAB allows ASIC to grant leave to persons who have been disqualified from managing corporations by ASIC under sections 206F and 206GAA of the Corporations Act, to manage select corporations. *[Part 3 of Schedule 1, item 27, section 206GAB]*

4.23 ASIC can determine any conditions and exceptions which it considers are appropriate, if it grants leave to a person to manage select corporations. *[Part 3 of Schedule 1, item 27, section 206GAB]*

4.24 ASIC previously had a power to grant leave to persons to manage corporations, if ASIC disqualified them for contravention of section 206F. Subsection 206F(5), which granted ASIC this power, has been repealed and incorporated into the new section 206GAB.

4.25 The legislative amendment to section 206F to repeal subsection 206F(5), requires a number of minor legislative amendments to the Corporations Act to update cross references which referred to the power to grant leave under section 206F. *[Part 3 of Schedule , items 20, 21, 22,*

23 & 24, subsection 201B(2), section 203B, subsection 204B(2), section 204G, and subsections 206A(1B) & (2)]

Section 1274AA: Register of disqualified company directors and other officers

4.26 Minor amendments are made to section 1274AA (the register of disqualified company directors and officers) to outline that ASIC's register of disqualified person must include:

- details of those persons disqualified by ASIC under section 206GAA;
- information on every notice of disqualification issued by ASIC to persons under subsection 206GAA(6);
- information on every permission ASIC has given to persons to manage corporations, under section 206GAB; and
- details of those person's disqualified by the Court under section 206EAB.

[Part 3 of Schedule 1, items 28, 29 & 20, paragraphs 1274AA(1)(a), 1274AA(2)(ab) & 1274AA(2)(c)]

Consequential amendments

4.27 There are no consequential amendments.

Application and transitional provisions

4.28 The provisions apply to events mentioned in subsections 206EAB(2) and 206GAA(2) that occur on or after the day five years before commencement of the provisions. *[Part 4 of Schedule 1, item 31, subsection 1649(1)]*

4.29 A permission given under subsection 206F(5) that was in force immediately before the commencement of the bill continues in force (and may be dealt with) as if it had been given under section 206GAB as inserted by the bill. *[Part 4 of Schedule 1, item 31, subsection 1649(2)]*