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AUSTRALIA + NEW ZEALAND

12 October 2020

Market Conduct Division
Treasury
Langton Crescent
PARKES ACT 2600
AUSTRALIA

By email: MCDInsolvency@Treasury.gov.au

Dear Sir or Madam,

## Insolvency reforms to support small business - Corporations Amendment (Corporate Insolvency Reforms) Bill 2020

Chartered Accountants Australia and New Zealand (CA ANZ) welcomes the opportunity to provide feedback on the Corporations Amendment (Corporate Insolvency Reforms) exposure draft (ED) and accompanying explanatory materials (EM).

**Appendix A** outlines our key points and detailed feedback on the ED, EM as well as the Government's *Insolvency reforms to support small business* factsheet (Government's factsheet). In developing our feedback, we consulted with our Insolvency Management Committee and other members in the insolvency profession. Further to this, we note that the majority of registered liquidators (RLs) in Australia are members of CA ANZ.

### Key Points

- We welcome these reforms which have the potential to curtail many future pain points for business. However, the complexity of these reforms will increase pressure on practitioners as they will be required to assist small business directors in comprehending all the implications for their business as well as to provide support to management during the process.
- We are concerned that this is a very limited consultation period for such complex reforms. Therefore, we strongly recommend the legislation includes a full and comprehensive review late next year to ensure the reforms are operating as intended and there are no unintended consequences.
- There is a high risk that the general public will not be able to distinguish between a RL and a small business restructuring practitioner (SBRP) with the establishment of a third class of RL. It is intended that the requirements for an SBRP are not to be as comprehensive as those to become a RL and, as such, it is important that there is a clear distinction between the two.
- We consider it critical that the standards, qualifications and experience of SBRPs are at an appropriately high level, backed by a commitment of professional ethics and standards. Relaxing these standards too much could quite easily lead to inconsistent approaches being taken and poor policy outcomes.



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Should you have any questions about the matters discussed above or wish to discuss them further, please contact Karen McWilliams via email at karen.mcwilliams@charteredaccountantsanz.com or phone (612) 8078 5451.

Yours sincerely

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# Appendix A

## General comments

CA ANZ welcomes these reforms as we have been calling for a Government response to the nation's impending insolvency cliff. These reforms provide necessary assistance during these difficult times and will offer viable businesses the best chance of survival. These reforms are complex and although they have the potential to curtail many future pain points for business, they also require very careful analysis and detailed feedback. The ED and EM are a critical component of the reforms, but much of the detail relating to the implementation will be in the subordinate legislation that is not yet available.

On face value, the proposed reforms appear to reflect the current voluntary administration (VA) process with the exception of the various creditor's meetings and the voluntary administrator's report required. The complexity of these reforms has raised concerns around the ability for small business directors to comprehend all the implications for their business. There will be added pressure for practitioners to provide support to management, while the director is still in control of the daily operation of the company, as well as guidance on the impacts of these reforms as a part of this process, which will inevitably lead to greater costs.

We are concerned at the short consultation period for such complex draft legislation. Further, the absence of the regulations and rules for respondents to consider at the same time has made it more difficult to fully understand the reforms and provide appropriate feedback.

We note the intended start date of 1 January 2021 and the need to have legislation and regulations drafted and passed prior to this date. This is an incredibly short timeframe. We strongly recommend the legislation includes a full and comprehensive review late next year (within 12 months) to ensure the reforms are operating as intended and there are no unintended consequences. In particular, ensuring that small businesses are using it effectively to restructure and there is no misuse of the process.

Our members have expressed concern that the legislation could be underutilised, or even ineffective if there are too many hurdles, complexities and challenges to businesses availing themselves of it. They note examples of Ipso Facto and to a lesser extent, the Safe Harbour regimes. Both of which have failed to have a significant impact on the market. A critical issue here will be for businesses to act early, while their debts have not accumulated to such a level that restructuring is no longer an option.

In this context, we have joined with other accounting and bookkeeping professional bodies, the Australian Small Business and Family Enterprise Ombudsman and the Council of Small Business Australia in calling for a government funded subsidy to ensure small businesses can access urgently needed professional advice on their viability. Under the jointly proposed Small Business Viability Review program, small businesses with up to $10 million in annual turnover would be eligible to obtain a subsidy valued up to $5,000 to access a tailored 15-month plan from an accredited professional on how and whether to turn around their business or exit.

## ED and EM feedback

### Chapter 1 - Debt restructuring

Whilst we support the concept that business owners will be able to trade in the ordinary course of business, we anticipate that many business owners will lack the necessary skills to be able to manage the ongoing trading of their business at the same time as handling numerous creditor claims and demands that will challenge them during the restructuring process.

Once the outside world is notified that a small business is proposing a debt restructuring plan, credit for the small business is likely to be shut off. The bank or financier may limit facilities, and suppliers may limit



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further supply, and/or put the company on cash on delivery terms. In respect of contracting businesses, a distressed business may struggle to win new contracts. In particular, in Queensland any construction business licensed under the Queensland Building and Construction Commission Act is likely to have their license cancelled and so they will have no chance of restructuring under this process.

As a result, we consider it is highly likely that the practitioner engaged in the process will need to provide at least a reasonable level of practical, day-to-day assistance to the business owners. The extent of such assistance could not be known at the start of the engagement, which is a clear issue in the context of determining the fee upfront.

According to reports filed with the Australian Securities and Investments Commission (ASIC),[1] the second most likely nominated cause of failure in the 2018/19 financial year was poor strategic management of business (as noted in 43% of reports). Therefore, despite the current pandemic conditions, creditors will naturally ask: 1) will things be different this time? and 2) how will the owners learn from past mistakes and implement real change and demonstrate this to creditors? If businesses cannot answer these questions comfortably, it is unlikely creditors will trust the owner/directors and continue to trade with them.

#### Entering the debt restructuring process

Section 1.15 of the EM outlines the process for appointment of a small business restructuring practitioner. We recommend that Schedule 453B1(b) is amended to refer to the "majority of" directors for consistency with the VA regime.

#### Eligibility Criteria

We note the eligibility criteria for the simplified liquidation process are detailed in section 3.19 of the EM and section 1.22 outlines the intention for the same criteria to apply to the debt restructuring process.

We support all these criteria for both the simplified liquidation and the debt restructuring processes and strongly encourage consistency in the eligibility criteria between these two processes.

### Report on company's business affairs

We support the requirement under S.497(4) of the ED for directors to provide the liquidator with a report about the company's affairs and a declaration that the company will be eligible for the process. For the debt restructuring process, s 453C(1) requires the liabilities test to be met on the day. We recommend this is enhanced such that the directors are required to complete a Report on the Company's affairs and property (ROCAP), which is then lodged with ASIC.

Additionally, we consider that for businesses to be eligible for this debt restructuring process, it will be critical that their financial books and records are up to date. However, the majority of small and medium-sized enterprises (SME) failures are linked to poor record keeping. Therefore, we recommend that the required status of records is addressed in the eligibility criteria as well.

### The liabilities test

We note the intention to prescribe the threshold amount in regulations. In our members' experience, the value of creditors almost always exceeds the initial estimate. It will be important for the new debt restructuring process to specifically address how this will be practically considered with respect to the threshold.

In supporting the reasonableness of the threshold, clarity around the underlying calculation will be needed. For example, will the calculation include secured, unsecured, contingent debts such as redundancy payments and damages claims (ie. breach of contract or breach of lease and future lease liabilities)?

[1] See https://asic.gov.au/about-asic/news-centre/find-a-media-release/2019-releases/19-363mr-asic-reports-on-corporate-insolvencies-2018-19/



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### Tax lodgements

We support the inclusion in the eligibility criteria of the requirement for tax lodgements to be up to date, but note that in practice, this maybe a significant barrier to entry. In our members' experience, many struggling businesses are delinquent with their tax lodgements and may have no idea of the quantum of tax debt owing. Remittances of employment entitlements (PAYG withholding and Superannuation Guarantee) are often also well overdue. Some struggling businesses are also likely to have suffered a breakdown in their commercial relationship with the accountant who in better times managed their tax affairs (i.e. restoring tax compliance can be both time consuming and costly).

We note that S.500AA(1)(f) of the ED states that 'the company has given returns, notices, statements, applications or other documents as required by taxation laws (within the meaning of the Income Tax Assessment Act 1997)'. For clarity, we recommend this is amended for the company to lodge returns etc with the ATO. Further, whether these returns and notices would need to be up to date as a part of the process.

Further, an avenue for directors to satisfy a Directors Penalty Notice (DPN) (under the type 1 notice where a director only has 21 days from the date of that notice to remit any director penalties stated on that particular DPN) could be by entering into a small business restructuring plan. We suggest the relevant provisions relating to DPN within the Taxation Administration Act 1953 (Cth) are considered with respect to their interaction with these reforms.

Section 1.17 of the ED states that the debt restructuring process is not available to a company if it is also under restructuring or administration, or with a deed of company arrangement that has not yet terminated. However, we question whether a company should be able to enter into a debt restructuring process if a winding up application has already been filed. The creditor would have gone to the expense of filing such an application and for the debt restructuring process to proceed, an application to the court would be required resulting in additional costs.

### Subsequent ineligibility

The legislation will need to be clear on the required process and associated consequences if, during the preparation of the plan, an amount exceeding the threshold is found to be owing. In determining this process, it is important to note that entering into the debt restructuring plan is an effective admission of insolvency of the company. It may be that in this instance, creditors or the court could terminate any agreed proposal and seek to put in place a mechanism to place the company into formal liquidation.

### Protections against misuse

The eligibility criteria, under S.453C(1)(b) of the ED, is not met when a director or past directors (12 months) have been involved with another company that has been under restructuring or been the subject of a simplified liquidation process (with a prescribed period). We welcome the intention to ban the same company directors from using the process more than once and the extension of this to former directors within the prior 12 months.

However there appears to be no indication about the number of times that a company can enter into a restructuring or liquidation process in S453B or S453C of the ED. There could be a risk that a company may enter into multiple processes at any given time. We understood according to the Government factsheet that this was to be limited for the company itself. We suggest that the company, as well as the directors are subject to the eligibility criteria.

In addition, directors have been known to resign immediately prior to a liquidator being appointed with a new director then appointed. In circumstances where the director has been a director of a company (or was previously a director of a company in the last 12 months) that has previously availed itself of provision S.453C (1)(b) of the ED, then consideration should be given as to whether the company should be ineligible.

Further, the interaction of this potential restriction on companies within a corporate group should be



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considered. For example, a director may operate a number of restaurants each through a separate company. If the group is in financial trouble, will only one company in the group be able to avail itself of these provisions?

### The Small Business Restructuring Practitioner (SBRP)

#### Who can register as a Small Business Restructuring Practitioner?

In section 1.30 of the EM, we note that only a RL can consent to be appointed, and act as, a SBRP. Upon further clarification from Treasury, we understand that the intention is for the accompanying regulations to establish the SBRP as a third class of RL.

There is a high risk that the general public will not be able to distinguish between a full RL and an SBRP with the establishment of a third class of RL. It is intended that the requirements for an SBRP will not be as comprehensive as those to become a RL and as such it is important that there is a clear distinction between the two.

We consider it critical that the standards, qualifications and experience of SBRPs are at an appropriately high level, backed by a commitment of professional ethics and standards. Relaxing these standards too much could quite easily lead to inconsistent approaches being taken and poor policy outcomes. The Government is already aware of the many risks surrounding untrustworthy pre-insolvency advisers taking advantage of vulnerable small businesses and it is critical that this new policy does not open up avenues for unscrupulous behaviour.

RLs have years of experience in dealing with various stakeholders and are able to quickly assess the financial position of a company and deal with those various stakeholder claims. These stakeholders include employees (including trade unions), the Australian Taxation Office (ATO) for PAYG and the superannuation guarantee charge, secured creditors over one or multiple assets, landlords, unsecured creditors and contingent creditors. For example, when paying a dividend to creditors, RLs will adjudicate a creditors proof of debt form and determine how much to admit the claim for. At times, this may not be a straightforward task.

In our opinion, the critical requirements will include:

- **The SBRP maintains adequate and appropriate professional indemnity insurance** – this is in relation to the onus we assume is carried by the practitioner with respect to their declaration to creditors in relation to the debt restructuring plan.
- **The SBRP has a sound knowledge of accounting and the Australian taxation system** – they will need to make an assessment on the financial position of the entity, determine its eligibility for the debt restructuring process, co-develop a restructuring plan and assist with execution of that plan.
- **The SBRP has an adequate understanding of Australian insolvency law** - the creditors in receipt of a restructuring proposal certified by a practitioner are likely to want some comfort that their financial return would not be better under the alternative outcome of liquidation. In order to make that assessment, the SBRP will need knowledge of the commercial issues associated with determining and assessing the quantum of potential antecedent transactions in a liquidation. Having an opinion of that made by a person with no practical knowledge or accountability for the subsequent pursuit of such recoveries would be high risk.
- **The SBRP would be a member of a professional association with a certificate of public practice (CPP) bound by an appropriate code of ethics and robust disciplinary process** – creditors will be relying upon the information provided to them by the SBRP and the creditability of SBRP. Creditors should rightfully expect that the SBRP giving such a certification would be of a reputable standing. Directors are also likely to be faced with conflicting demands and ethical dilemmas that the SBRP may need to oversee - for example requests from key suppliers to agree to the return of stock and then the re-invoicing of it on cash on delivery (COD) terms as a condition of interim support and post restructuring support. The SBRP would also need to be independent from the small business entity and the owners.



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Accounting is the only professional system with the necessary background in ethics, trust and expertise that also provides consumer protection with professional indemnity insurance. Over 80% of existing RLs are also Chartered Accountants. To this end, **Appendix B** provides further information on Chartered Accountants and their core level of expertise and professional standing. We consider that Chartered Accountants, who hold a CPP and have relevant experience with restructuring and advising businesses, would have the necessary skills, capability and experience to register as SBRP.

### Training and registration

Existing RLs will need time to familiarise themselves with the new legislation, re-visit current processes and up-skill their workforce. However, they are likely to be the main professionals registered as at 1 January 2021. Additional professionals registering as SBRPs will need time to obtain any necessary training and register with the appropriate regulator. Any specific training or qualifications required, will need to be developed between the passing of the legislation and the commencement of the reforms.

### ASIC fees

We anticipate that the new SBRP role will also be regulated by ASIC. ASIC will therefore require the necessary funding to support this new regulatory function. However, there is also no indication in the Government Factsheet of the fees that will be charged with respect to the application, registration and Industry Funding Mechanism (IFM) charges for the new SBRP. It is important that SBRPs are subject to similar regulatory fees to those imposed on RLs, albeit commensurate to their reduced classification and scope, to ensure a fair and competitive market.

We anticipate that there will be additional regulatory activities and costs that will be required to ensure SBRP compliance, particularly in the first few years. It will be important for ASIC to separate the additional SBRP compliance costs from the existing RL monitoring and enforcement, particularly for the first few years. This separation will allow for clear identification of costs and issues (separate from pre-existing RLs) that can be appropriately considered in the IFM.

### Independence of SBRP

We support the requirements in Section 1.31 of the EM, to ensure the independence of the SBRP. It would be expected that the practitioner is independent of the directors to fulfil that role of trust that creditors will expect. However, the level of operational management support that may be required could blur the independence which the policy seeks. So although there will be an oversight role provided by the practitioner as a part of the process, it will be important that it is recognised that this will not impact the independence that creditors expect of the process.

### Effect of things done during restructuring of company

We note that S453M will require the professional judgment of the SBRP. It is possible that a transaction entered into is in the best interests of some creditors but not others. In these circumstances, consideration needs to be given as to whether it is overall in the best interests of creditors. Any payments signed off by the practitioner, will be valid and not liable to be set aside in a winding up. An SBRP will require significant experience to make these decisions, given under S453H, there will be no liability for these decisions.

We question whether applications to the Court to challenge decisions or transactions entered into should be able to be made by ASIC, a liquidator appointed to the company, creditors (consider whether there should be a minimum percentage of debt compared to total debt owed by the company) or members (again with a certain minimum percentage of shared held).

S453H states that the restructuring practitioner acts as the company's agent. This carries added risk for the practitioner where they have no control over the business itself as it is left in the director's hands. This is in some way addressed through the consent required by the practitioner to transactions outside of the



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ordinary course of business. However, there is the potential for this to conflict the practitioner out of subsequently becoming the liquidator if the proposal is not accepted.

### Restructuring practitioner may terminate restructuring (453J)

In the event that a restructuring practitioner terminates the restructuring for a company, there is no indication in the ED/EM that outlines what happens to the company after this termination occurs. We suggest that the determining whether control would pass back to the directors in these circumstances or if there would be an automatic liquidation would need to depend on the rationale for the termination.

### Personal guarantees

Section 1.60 of the EM notes that entering the debt restructuring process is not to trigger liability of directors or relatives for guarantees of the company's liability. Currently the period this relates to is unclear as s453V of the ED states 'during the restructuring of a company…' This could be taken as meaning that the personal guarantee cannot be called upon whilst the dividend payment process is progressing, which could extend quite some time. We recommend this is limited to the "restructure period" ie. up to the date when creditors make a decision on the restructuring plan.

Further, we question how this process will practically ensure that SME businesses can continue to trade and operate when any compromised debts will remain subject to personal guarantees (provided to the vast majority of commercial creditors, who will no doubt expect payment of the shortfall) and the ATO will presumably retain its ability to issue a Director Penalty Notice (DPN) post the restructure for outstanding GST and PAYG? The majority of SMEs are family businesses or intrinsically financially linked to the directors of the SME, the bankruptcy or personal financial distress of the director will likely have a negative impact on the ultimate success of this process and be a barrier to both entry and success.

### Terminating a debt restructuring process

Section 1.84 of the EM notes that the circumstances under which a debt restructuring of a company ends may be prescribed by the regulations. For clarity, does this mean that a SBRP could veto a restructuring plan before it is presented to creditors?

Further, we recommend that this includes the SBRP will having the power to stop the process where misconduct is identified. There will also need to be clarity around the process if misconduct is found before the approval of the plan as well as after the approval of the plan. The creditors may not have accepted the proposal, had they known about the misconduct. Further, who is responsible for reporting the misconduct?

### Communication with creditors

We note the intention under S.457B of the ED that the company is responsible for including a notice in public documents that a restructuring practitioner has been appointed and S.453D of the ED for the SBRP to make a declaration regarding their appointments. However, at the commencement of the 20-day debt restructuring process, we consider there will need to be clarity around who is responsible for notifying creditors of the commencement of the process. We suggest that the SBRP should be the person given this responsibility to ensure it occurs in a timely manner. Consideration will also need to be given as to whether this communication will be public, and hence whether all ongoing creditors will be aware of the company status.

There will also need to be clear guidance as to what information, at a minimum, is given to creditors. As noted earlier, in particular, the plan will need to be compared to the return creditors would get in a liquidation and comment with respect to recoveries available in a liquidation. Whilst it might be assumed in the early restructures under this process that most debt would be incurred during the COVID-19 moratorium period, in many cases this may not be the case. There are a number of small businesses who were carrying a lot of debt pre-COVID-19, particularly due to the ATO.

### 20-day plan development period

The legislation indicates that the directors remain responsible for the company during the restructuring



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period and therefore we assume they will be responsible for debts incurred during the 20-day period whilst the plan is developed. In a VA process, the VA personally guarantees the debts such that creditors remain willing to continue to provide credit to the distressed business during the period. Therefore, clarification will be needed as to the treatment of any additionally incurred debts during this period under the plan and who will guarantee them? We support the inclusion of requirements for the directors to responsibly manage the company during the restructuring period.

Likewise, the treatment and guarantee of debts during the 15-day period for the creditors vote will also need to be considered. Combined with the 20-day plan development period, we note that the total of 35 days exceeds the current VA process.

### Restructuring plan extension

In practice, there may be instances where additional information is required or key stakeholders are unavailable (e.g. office shutdowns, public holidays) which may impact the restructuring plan development and finalisation. We suggest an acceptable time extension should be considered for the 20-day period. However, if such an extension would be approved through a Court, this would go against the intent of the process, which is to be short and low cost.

### Practitioner declaration to creditors of the plan

We note section 1.50 of the EM refers to the SBRP '*giving an opinion on feasibility of a proposed plan in their declaration'* and Schedule 453E(1)(c) of the ED includes '*to make a declaration to creditors in accordance with the regulations …'* under the functions of the SBRP. Further the Government's factsheet states that '*The practitioner sends the plan and supporting document to creditors and certifies whether they consider the business can meet the proposed repayments and has properly disclosed its affairs.*'

We are concerned with the open ended and comprehensive nature of the proposed certification within the Government factsheet. This is potentially akin to underwriting the plan, giving rise to both substantial impracticalities and the likelihood of distorted creditor decision making. The main reasons for our view include:

- It is unlikely that appropriate practitioners would be willing to take on the proposed role or be able to secure professional indemnity insurance for such engagements. The proposed certification would result in substantial risk regarding future events associated with the plan and the veracity of disclosure of affairs. Practitioners would encounter substantial practical difficulties in forming a conclusion on such matters in the context of the proposed engagements.

- Creditors may be swayed by the existence of the certification whether or not this is in their best interests, rather than a process where directors must genuinely convince creditors of the merits of the plan and their own credibility – a key facet of any debtor in possession model. This may lead to the widespread adoption of plans that ultimately exacerbate rather than mitigate the economic impacts of distressed businesses.

- We are particularly concerned about the use of the term 'certify' in the factsheet, which may imply assurance or an attestation that goes beyond the level of comfort involved in an audit or assurance engagement. Limited or reasonable assurance as defined by standards issued by the Auditing and Assurance Standards Board is not possible within the proposed timeframe and the information and cost constraints of the SBRP role, let alone a higher level of attestation.

- The proposed certification goes significantly beyond what is required in a VA report to creditors – both in terms of including statements about future events (i.e. meeting proposed repayments) and concluding on disclosure of affairs. Moreover in a VA situation, the administrator would have likely had substantially greater time and access to assess the company in order to deliver a more contained, caveated report, in which the VA will provide an opinion as to what is in the best interests of creditors from the 3 options available, than what is proposed for the certification.



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- The role of a practitioner in advising, consulting and aiding in the compilation of the plan could conceivably lead to conflicts of interest and a lack of independence in then offering a certification on the same plan.

When the subordinate legislation is drafted, we recommend the following alternative approach that would address these impracticalities and better reflect the nature of the SBRP role:

- A statement by the SBRP describing their role, clearly setting out the role's limits and relevant information constraints, and a statement on the process of compilation of the plan in accordance with the applicable requirements.
- A statement by directors describing their role in relation to the plan and the disclosure of affairs, highlighting the key assumptions involved and their ultimate responsibility for the plan.

### Employee protections

Section 1.95 of the EM refers to the potential for regulations to include certain criteria and includes an example for the requirement of the company to pay employee entitlements before the plan can be put to creditors. It is critical for employees to be protected in this process and payment of employee entitlements must include superannuation. Although we question whether those small businesses commencing this process will be in a financial position to pay any due and payable employee entitlements.

We note, however, the impact that Single Touch Payroll (STP) is having on accountability for employee superannuation and we are keen to explore the interaction of STP reporting with this policy proposal as well as broader revenue protection safeguards such as Director Penalty Notices. There is also the interaction with the Fair Entitlements Guarantee scheme to consider.

A business commencing the restructuring process may also experience employees leaving, with their accrued entitlements, while they can. This could put greater pressure on the cashflow of the business.. We suggest consideration of an appropriately structured guarantee of payment of outstanding employee entitlements to provide flexibility for those businesses that maybe struggling to satisfy this eligibility criteria.

### Voting

The regulations will need to address the voting criteria. We note that the Government factsheet indicates that plan will pass if more than 50% of creditors by value endorse the plan. In comparison, the recent Business Debt Hibernation process in New Zealand requires 50% of creditors vote by value <u>and</u> by number.

Additionally, the *Insolvency Law Reform Act 2016* (ILRA) was, in part, introduced to harmonise the personal and corporate insolvency provisions and to a large degree has done that with voting. It would therefore be disappointing to move away from that harmonisation by introducing a new criteria to pass a resolution under these proposed reforms when IPR 75-130 provides a mechanism to pass a resolution without a physical meeting; being greater than 50% in number and dollar.

In relation to creditors voting, similar to other elements in insolvency, it could be best to include that those creditors who may have purchased debts in relation to the company are able to vote only to the extent of the amount for which they purchased the debt. This can prevent vote stacking by interested parties guaranteeing a "return" to creditors of sorts (by purchasing the debt) and then using the full amount of the existing claim to influence the vote. This may not be as relevant with related creditors being unable to vote, but it might be worth a thought.

We welcome the prohibition on related parties voting as indicated in section 1.8 of the ED. Additionally, we note the intention in the Government Factsheet that secured creditors are only entitled to vote to the extent that they are unsecured. Therefore, it would not be inconceivable that the actual vote being considered for acceptance could be based on creditors with value much less than $1,000,000. We also consider it highly likely that the ATO could represent a significant portion of that voting value.



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This would place a very high responsibility on the ATO to consider and respond to voting within the 15 day period on a large number of small business restructuring requests. This would significantly increase the workload for the ATO, who would need to be appropriately resourced to respond to these requests in a timely manner. We also consider there is the potential that the ATO's decisions regarding the plans and remuneration could become central to the entire process.

**Exiting the debt restructuring process**

### Plan voted down

The regulations will need to address what may happen if the plan is voted down. The Government factsheet indicates that the process ends and the company owners may opt to go into VA or use the simplified liquidation pathway. In order to keep the process simple and minimise costs, we strongly recommend that the company should automatically be placed in liquidation if the plan is voted down. This whole process is designed to deal with a small business with serious financial issues given under S453B1(b)(i) the directors have declared the company insolvent or likely to become insolvent. Therefore, by having the debt restructuring plan rejected, the company should then proceed to be placed into liquidation. If eligible, this could be the simplified liquidation pathway.

However, we note that page 9 of the factsheet indicates that the role of SBRPs will be limited to the debt restructuring process. Therefore, if an RL developed the restructuring plan, clarity is needed as to whether they could also administer the liquidation process. There may be concerns regarding independence for the same practitioner to act in both circumstances, however there would be an additional cost burden to change practitioners at this stage.

Under the *Corporations Act 2001*, RLs are required to lodge Declarations of Independence and Relevant Relationships and Declarations of Indemnities (DIRRIs) with ASIC after being appointed. A similar process could be adopted if it considered practical, to allow for a RL who has developed the restructuring plan to continue to carry out the liquidation process.

### Plan fails

The Government's factsheet does not currently cover the process to be followed if the restructuring plan is approved but subsequently fails. Similar to our views on the plan being voted down, in this situation the regulations should include a requirement for the company to enter liquidation. This is critical to ensuring the best possible plan is proposed to creditors and ensuring their losses don't accumulate further through a prolonged process. Additionally, clarity will be needed as to how payments to creditors made under the restructuring plan will be treated with respect to preferences, if the plan subsequently fails. Our comments above seeking clarity as to whether the same practitioner could be appointed to a subsequent liquidation, if they were an RL, are relevant here.

**Interaction between sections of the Act and other legislation**

S.453M of the ED outlines when a payment is made, or transaction entered into (or other) in good faith while a company is under restructuring that it is valid and effectual for the purposes of the Act. However, in S.455A of the ED, the company is taken to be insolvent once a restructuring plan has been proposed. This is conflicting information and we suggest that the interaction between sections, such as this, is clearly outlined in the Act.

As noted above, once a company proposes a restructuring plan it is considered to be insolvent (S.455A of the ED). Director safe harbour measures protecting from insolvent trading should be reviewed to determine how these protections interact with the timing of when a company is considered insolvent under this reform.



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## Chapter 2 - Temporary relief for companies seeking a restructuring practitioner

We note the exposure draft of these temporary relief amendments are not yet available for consultation. In the Government's fact sheet, the proposed concept is to give creditors three months' notice of an intent to enter a restructuring procedure. This will, in all likelihood, bring an end to the capacity of the company to trade through the transitional period. Creditors will assert their rights to (eg to recover stock not paid for) and refuse to extend credit to an organisation they now know to be insolvent and with an uncertain future.

Whilst we understand and appreciate this well-intentioned proposal, we recommend this is removed as it will not have the desired effect and is not commercially viable.

We also consider it important that Government encourage businesses to seek advice early and not wait until the end of the temporary relief measures on 31 December 2020. The longer businesses wait to obtain appropriate professional advice, the more their debts will accumulate further deteriorating their financial position.

## Chapter 3 - Simplified liquidation pathway

### Eligibility criteria

We support the eligibility criteria under section 3.19 of the EM and have provided additional comments with respect to these criteria within our comments on debt restructuring process above which are also relevant to the simplified liquidation pathway.

Section 3.26 of the EM and S.498 of the ED allow 5 days for the directors to provide the declaration to the liquidator. Five business days seems excessive and may result in unnecessary delays. We encourage consideration of instead requiring this to be provided at the same time as the passing of the resolution for the voluntary winding up is passed.

Section 3.30 of the EM indicates the declarations the directors should make regarding the company's eligibility for the simplified liquidation process. We recommend that there is clarity as to whether a company can enter into the simplified regime after attempting a debt restructuring plan.

### Exclusions for entering the simplified liquidation process

Section 3.53 of the EM states that *The liquidator must not adopt the simplified liquidation process if at least 25 per cent in value of the creditors request the liquidator not to follow the simplified liquidation process in relation to the company (the 25 per cent test*). We note that in section 3.56 of the EM, the regulations can prescribe creditors which are, or are not, to be taken into account for the 25 per cent test. We recommend that related party creditors are excluded.

### Features of the simplified liquidation process

S.500A (3) of the ED indicates that the liquidator must give written notice to each member and creditor of the company. We understand the intention of the simplified liquidation process is to create a more efficient process for small companies (Section 3.58 of the EM) but these notification requirements may in fact increase the costs of the liquidation, noting that members also have to be notified. It is not uncommon for creditors who are not listed in the company's records to let the liquidator know of their claim sometime after the process has started. In many cases the books and records of a small business are poorly kept. We suggest considering the size of the creditor (i.e. 5% of the creditor pool) as a part of this requirement.

The new streamlined liquidation process appears to fundamentally differ from the current voluntary liquidation process through the reduction of investigation and reporting requirements (S.533 of the ED) and reducing meetings. However, it appears that the requirements to report to creditors – Initial Report and Statutory Report, remain unchanged and section 3.64 of the EM indicates that the regulations will



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prescribe rules around alternative reporting to ASIC. Therefore, we consider that the costs savings associated with the reduced requirements will be minimal.

S.500AB of the ED provides that a creditor may at any time give the liquidator of a company notice in writing requesting the liquidator not follow the simplified liquidation process in relation to the company. However, the ED appears silent on the actions of the liquidator on receipt of the notice. S.500 AB seems inconsistent with S.500A(2)(c) of the ED which provides an opportunity to creditors holding at least 25% in value to direct a liquidator not to adopt the simplified liquidation process (within a specified timeframe). We recommend that related party creditors are excluded from the calculation of the 25% under S.500A(2)(c) of the ED.

In addition, there could be potential implications of S.500 AB assuming the RL is required to act on the notice, including:

- The RL agreed to an upfront fee on the basis of the simplified process and are now doing the more complicated process, incurring most costs for which they are unlikely to be paid.
- The RL pays a dividend under the simplified process and then has the imposition of the more costly liquidation imposed upon them with no funds to meet those costs.
- A creditor requires the conversion for no specific reason.

We suggest further consideration of the implications of S.500AB of the ED and if this section is practically appropriate.

### Unfair preferences

Section 3.73 of the EM provides for regulations to provide circumstances in which a transaction is not an unfair preference or a voidable transaction for the simplified liquidation process. The ATO is a key agency for insolvency practitioners in this context. We await the draft regulations to understand how the new policy will impact the RL's ability to lodge, substantiate and seek recovery of unfair preference payments.

## Chapter 4 - Refinements to the registration of liquidators

We note the additional flexibility granted to the committee to approve a registration despite particularly criteria not being met. The knowledge, experience and standards of a RL must be of a high standard and it is critical that the integrity of the profession is preserved.

## Chapter 5 – virtual meetings and electronic communications

We support the changes to make key parts of the Corporations Act technology neutral to enable more efficient external administrations.

## Further measures to support the system

### IFM Fee waiver

We note the intention in the Government factsheet to temporarily waive the fees associated with registering as an RL. However, ASIC's industry funding model (IFM) is not currently considered in these reforms.

Most RLs work in small businesses themselves – small one to three partner businesses which are, generally, not highly profitable (liquidators earn up to 30% less than their equivalents in tax or audit). These small firms also deal with the vast majority of SME insolvencies in Australia. They are also those affected the most by the IFM.

As you will be aware, COVID-19 has dramatically worsened the insolvency market and surveys by the Australian Restructuring, Insolvency and Turnaround Association (ARITA) indicate some 55% of insolvency firms are currently on JobKeeper. Many insolvency firms are now in significant financial distress themselves. It is also important to note that insolvency practitioners are the major providers of



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business restructuring advice and will form the core group of professionals best placed to implement these new reforms from 1 January 2021.

However, RLs will also have to pay the still unknown amount of the ASIC IFM for the 2019/20 financial year in January 2021. It is expected to cost upward of an average of $14,000 per liquidator but may vary from $5,000 to upwards of $40,000. Liquidators remain unsure exactly how much they owe because the metrics have still not been finalised.

We strongly advocate to Treasury and Government to temporarily waive the IFM fees for RLs for the previous and current financial years.



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# Appendix B

## Why choose a Chartered Accountant?

Across the country, in local communities and large cities, Chartered Accountants are seen as a trusted and educated group of financial professionals who are working every day to serve the interests of all businesses in the Australian economy.

This is a result of:

### Being highly qualified

As well as relevant degree-level study, all our members have completed a minimum of three years approved and mentored relevant work experience. Chartered Accountants have a TEQSA approved AQF8 post-graduate qualification which requires long hours of rigorous study.

### Significant continuing professional development obligations

Significant on-going professional development requirements ensure Chartered Accountants skills and knowledge remain current and relevant. Members are required to complete a minimum of 120 hours of relevant training during a three year period. This is monitored through audits for a selection of members as well as annual declarations from all members.

### Broad experience

Our members are accountants who can offer far more than technical knowledge. Chartered Accountants are broadly experienced in dealing with business and financial issues across a diverse range of management and advisory roles. This bigger picture holistic perspective enables them to work flexibly to positively impact businesses, organisations and communities.

### Fully accredited

Our members have all met, and are bound by, internationally recognised technical and ethical standards. Chartered Accountants ANZ is part of the Global Accounting Alliance - the coalition of the world's premier accounting bodies.

### Future-focused

Whether working in business or practice, Chartered Accountants are uniquely positioned to offer advice that can be trusted. Through deep understanding they have the skills to examine the past and guide organisations into the future.

### Highest ethical and professional standards

Members are required to adhere to a strict code of ethics included in the Accounting Professional & Ethical Standards Board's Code of Ethics for Professional Accountants (including Independence Standards) (APESB 110). They are also required to comply with detailed CA ANZ regulations which maintain high levels of professional standards.



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### Protection to consumers and members through the Professional Standards Scheme

All members in public practice must meet the requirements of the CA ANZ Professional Standards Scheme. This includes having minimum levels of professional indemnity insurance and appropriate disclosure of the limitation of liability under the scheme. This offers protection to both our members and their clients.

### Quality Review Program

The Chartered Accountants Quality Review Program reviews practices on a cyclical basis and examines each practice's compliance with technical and professional requirements, including compliance with the professional standards scheme. The programme monitors whether our members in public practice have quality control systems in place to ensure they comply with the Code of Ethics, professional standards, and legal and regulatory requirements. All members offering services to the public are eligible for review. This helps maintain a consistently high standard of quality and service to their clients.

### Conduct and disciplinary processes

There are robust disciplinary processes to hold members to account who may not comply with high professional and ethical standards. This includes investigating and resolving complaints made against members. Sanctions imposed on members can include termination or suspension of membership, a reprimand, training and costs.



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# Appendix C

## About Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand (CA ANZ) represents more than 125,000 financial professionals, supporting them to build value and make a difference to the businesses, organisations and communities in which they work and live.

Around the world, Chartered Accountants are known for their integrity, financial skills, adaptability and the rigour of their professional education and training.

CA ANZ promotes the Chartered Accountant (CA) designation and high ethical standards, delivers world-class services and life-long education to members and advocates for the public good. We protect the reputation of the designation by ensuring members continue to comply with a code of ethics, backed by a robust discipline process. We also monitor Chartered Accountants who offer services directly to the public.

Our flagship CA Program, the pathway to becoming a Chartered Accountant, combines rigorous education with practical experience. Ongoing professional development helps members shape business decisions and remain relevant in a changing world.

We actively engage with governments, regulators and standard-setters on behalf of members and the profession to advocate in the public interest. Our thought leadership promotes prosperity in Australia and New Zealand.

Our support of the profession extends to affiliations with international accounting organisations.

We are a member of the International Federation of Accountants and are connected globally through Chartered Accountants Worldwide and the Global Accounting Alliance. Chartered Accountants Worldwide brings together members of 13 chartered accounting institutes to create a community of more than 1.8 million Chartered Accountants and students in more than 190 countries. CA ANZ is a founding member of the Global Accounting Alliance which is made up of 10 leading accounting bodies that together promote quality services, share information and collaborate on important international issues.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents more than 870,000 current and next generation accounting professionals across 179 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications.



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