Law Council
OF AUSTRALIA

Business Law Section

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Corporations Amendment (Corporate Insolvency Reforms) – subordinate legislation

This submission concerning the draft *Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020* (**Regulations**) and the draft *Insolvency Practice Rules (Corporations) Amendment (Corporate Insolvency Reforms) Rules 2020* (**Rules**) is made by the Insolvency & Restructuring Committee of the Business Law Section of the Law Council of Australia (the **Committee**).

Regulations

No	Regulation	Comment
1	5.3B.03(1)	For the purposes of paragraph 453C(1)(a) of the Act[1], the test for eligibility is that the total liabilities, other than contingent liabilities, of the company on the day the restructuring begins must not exceed $1 million. This still would potentially allow for additional liabilities that were contingent upon an insolvency event crystallising upon the appointment of the restructuring practitioner (**RP**) and no-longer being contingent, which may push a company over the $1 million threshold. Although this will be reduced to some extent by the ipso-facto laws, the laws still only apply to contracts entered into on or after 1 July 2018 and they have various carve outs. If the test excluded any liabilities which were contingent immediately prior to the appointment of the RP, then that would deal with this issue.

[1] References in this submission to the Act are references to the *Corporations Act 2001* as will be amended by the *Corporations Amendment (Corporate Insolvency Reforms) Bill 2020.*

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No	Regulation	Comment
		Given that only contingent liabilities are excluded, it appears that the test will include future liabilities (noting that, under section 553 of the Act, all claims against a company (present or future, certain or contingent, ascertained or sounding only in damages), being debts or claims the circumstances giving rise to which occurred before the relevant date, are admissible to proof against the company). Therefore, liabilities that have been incurred but which will become payable in the future, will be included in the calculation. This will include future rent payable under a lease for the balance of the term where the obligation to pay it cannot be avoided (such as by exercising a 'break clause'). See *Russell Halpern Nominees Pty Ltd v Martin* [1987] 10 ACLR 539 at 541-542 (per Burt CJ) and *Shepherd v Australia & New Zealand Banking Group Ltd* (1996) 20 ACSR 81 at 89 (per Bryson J). It is difficult to know whether the data from ASIC that Treasury is relying on about the percentage of companies with liabilities of less than $1 million includes such future amounts owing in those liability figures.
2	5.3B.04(2)(a)	For the purposes of subsection 453L(4) of the Act, Reg 5.3B.04 prescribes the circumstances in which entering into a transaction or dealing by a company is not to be treated as being in the ordinary course of the company's business. The circumstances include that the transaction or dealing is for the purposes of satisfying a debt or claim in relation to the company, other than a contingent debt or claim, **that arises because of a contract or an arrangement entered into by the company before the restructuring of the company begins**. In order to pay these, the RP will have to consent (section 453L(2)(b)) or the court will have to consent (section 453L(2)(b)). There will often be these types of debts or claims that a company will need to pay in order to continue to trade (critical vendors who will not supply without earlier debts being paid). Is it the intention that an RP will have to consider these requests and approve them?

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3	5.3B.12 5.3B.16 5.3B.19 5.3B.22	Reg 5.3B.12 sets out the eligibility criteria for a restructuring plan. It requires in (1)(e) that eligibility be assessed as "immediately before the restructuring practitioner gives the plan and certificate in accordance with regulation 5.3B.19, regulation 5.3B.22 is satisfied in relation to the company." Reg 5.3B.22 is satisfied if employment entitlements have been paid and tax filings are up to date. Reg 5.3B.16 requires the RP to make a statement in a certificate as to whether the eligibility criteria have been met. However, the criterion in Reg 5.3B.12(1)(e) cannot be satisfied until after the certificate has been finalised and then given to creditors. Even if the threshold time were at the point of the RP making the statement under Reg 5.3B.16, that presents problems for the RP if there has been any time at all between execution of the plan and the RP's assessment of it, because there will be limited knowledge of what has happened in respect of wages, superannuation, BAS and other filings, etc. in the intervening days. Perhaps to achieve the requisite policy, Reg 5.3B.12 should read "immediately before the ~~restructuring practitioner gives~~ company executes the plan ~~and certificate~~ in accordance with regulation 5.3B.12(1)(b)~~19~~".
4	5.3B.16(4)	This offence provision appears too harsh. Consider whether the requirement should be if the RP does not believe, or there are no reasonable basis to believe, that the matters certified are true. There should also be an equivalent of section 189 of the Act for the RP.
5	5.3B.19(1)(a)(ii)	Are the restructuring plan standard terms those referred to in Reg 5.3B.25? If so, this should be made clear.
6	5.3B.25(1)(e)(i) and (ii)	There are various issues that these provisions will create. Under (i) the secured creditor could nominate a low value for its security, prove for its expected shortfall and receive a dividend in respect

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		of it and then subsequently realise the security for much more. Under (ii) the company, RP and the creditors will not know how much the secured creditor will receive under the plan until the secured property has been sold. It may be that a secured creditor has a substantial shortfall upon a sale, which is much greater than the company, the RP or the creditors thought and suddenly they have a very large claim which eats into the funds available for creditors. If the other creditors had known of the size of the shortfall, they may not have voted for the plan. It also means that unsecured creditors don't really know what their return under a plan may be - they may know what the amount available in total to creditors will be, but not know what the dividend to them will be and so it will make it more difficult for them to consider the plan and vote. A possible solution to this could be if secured creditors were required, in response to a request under 5.3B.19(1)(b), to provide and verify an estimate of the value of their security. Reg 5.3B.14 only requires the restructuring proposal statement to include a schedule of debts and claims, but it does not require that to include a statement of the company's understanding of the value of any security held. It would be good if it had to do that and the basis for that understanding. This would give creditors a better understanding of the amount that a secured creditor would be able to be a creditor for under the plan. If such an amendment was made, reg 5.3B.20 should be amended to allow the secured creditor or other creditors to object to the value attributed to the security. If this objection process leads to a significant amendment to the attributed value, the RP would have to give notice to the creditors. Secured creditors may argue that they will have to disclose market sensitive information about the value of their security if they disagree with the value the company has nominated for it and should not be made to disclose valuation information. If they are concerned about that they can either not object or object by arguing their security has a higher value (which will be in the interests of other creditors). If they do not object, they should not be taken to have

No	Regulation	Comment
		agreed with the value, but rather have agreed to accept it only for the purposes of the amount they are to be considered an unsecured creditor for the purpose of the plan.
7	5.3B.28	Delete the word 'organisation' from the heading. Under subclause (2)(b), a person bound by the plan cannot: "(b) proceed with such an application made before the plan became binding on the person." This is quite an impediment and stricter than in a voluntary administration, where the court has the ability to adjourn the application if it is in the interest of creditors. It will mean that many debtors of eligible companies will use the restructuring process to avoid pending winding up applications.
8	5.3B.30(1)(d)(ii)	Suggest the period of 30 business days be reduced to 20 business days. Thirty business days seems like a very long period for a person to have to rectify any default. The longer period that the default can be rectified, the longer the period until the plan may be terminated (if the default is not rectified) and the longer affected parties may continue to deal with the entity where ultimately the plan may be terminated and the company then wound up.
9	5.3B.44(2)(a)	This will likely require the directors to obtain legal advice or advice from a registered liquidator on this before they can make the declaration. This will add to the cost of the process.
10	5.3B.47(b)	While it is reasonable for the time to notify creditors to be 5 business days, there is no reason why the ASIC lodgement cannot be done sooner. This could be within one or two business days.
11	5.3B.49(1)(b)	As above
12	5.3B.49(2)(b)	As above
13	5.3B.51(3)(b)	As above
14	5.5.02	This will likely require the directors to obtain legal advice or advice from a registered liquidator on this

No	Regulation	Comment
		before the can make the declaration. This will add to the cost of the process.
15	5.5.04	We understand that the intention of this regulation is to only allow unfair preferences if the transaction was entered into within three months of the relation-back day and the transaction was for $30,000 or more. We find the drafting of this regulation difficult to follow and this was not the meaning that we first thought the regulation was intended to have. We recommend re-drafting to make it clearer.
16	5.5.08	There should also be a requirement to notify creditors within 5 business days of the decision to cease to follow the simplified process.

Rules

We have no comments or suggested amendments about the Rules.

The Committee would be pleased to discuss any aspect of this submission. Please contact the chair of the Committee Scott Butler on Scott.Butler@hallandwilcox.com.au or 07 3231 7722, if you would like to do so.

Yours faithfully

Greg Rodgers
Chair, Business Law Section