SHOPPING CENTRE
COUNCIL OF AUSTRALIA

23 November 2020

Manager
Market Conduct Division
Treasury
Langton Crescent
PARKES ACT 2600

Via email: MCDInsolvency@Treasury.gov.au

EXPOSURE DRAFT: CORPORATIONS AMENDMENT (CORPORATE INSOLVENCY REFORMS) REGULATIONS 2020

Dear Sir or Madam

Thank you for the opportunity to provide a submission on the *Exposure Draft Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020*, scheduled to commence on 1 January 2020.

While we flagged this issue in our submission on the Exposure Draft Bill, we put on record our disappointment that Treasury has provided an incredibly short timeframe for consultation.

As you are aware, the SCCA represents Australia's major shopping centre owners and operators.

We engage across all relevant policy and regulatory issues impacting our sector including retail lease legislation, competition and consumer law, along with issues such our current application to the ACCC to reauthorise our Casual Mall Licensing Code of Practice. In this regard, we are able to 'tie together' several areas of policy and regulation, along with our experience of remaining open during COVID-19 as an 'essential activity'.

Our key message and plea to Treasury is given shopping centre owners have, like the temporary loosening of insolvency laws, been a strong part of the 'relief' effort for small retailers (almost $2 billion in rental assistance provided under the Prime Minister's Code of Conduct announced on 7 April 2020) including keeping otherwise healthy businesses from going into liquidation, it is greatly concerning that we will stand to be severely adversely affected by these reforms including from unintended consequences whereby large firms will be able to use and game the new regime.

Amendments are need to the Draft Regulation to ensure a fair approach.

The largest category for our rental assistance correlates to those SMEs that have been the most affected by government restrictions including cafes, restaurants, and retail services such as hairdressers and beauty salons.

Retail has been particularly impacted by government restrictions, unlike other sectors such as the office and industrial leasing sectors.

It is greatly concerning that while having been part of the relief effort, shopping centre owners stand to be severely adversely impacted by these reforms.

This submission makes several recommended amendments to the *Exposure Draft Regulations* for Treasury's consideration.

As we noted in our submission to the Exposure Draft Bill, we are pleased that the focus of the corporate insolvency reforms is to assist small business by providing a simplified and streamlined opportunity to attempt debt restructuring for business continuity. We also noted that much of the detail for the proposed regime would be deferred to future Regulations.

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We are however extremely concerned that the proposed regime, including the Draft Regulations, will create **unintended adverse consequences** and cause harm in the retail market including to the detriment of shopping centre owners.

Two key points arise.

First, by failing to protect the ability of landlords to receive post restructuring rent and other occupancy costs under continuing leases, the Regulations, as drafted, place the burden of a restructuring regime on the shoulders of landlords. It is trite that a landlord should be entitled to receive rent for so long as it is required to lease the land. Second, while the reforms are also targeting 'small business', the reforms will also be able to be gamed by much larger businesses given how their entities are structured.

The fact that the reforms can be used and gamed by large businesses is in conflict with the regime's stated purpose, which is targeted at small business.

We don't believe these consequences are fair, have been properly considered, or are wholly consistent with the purpose of the insolvency reforms including being part of the Government's *JobMaker* package.

This includes how the insolvency laws are interrelated to the other *JobMaker* measure, 'removing barriers to credit', given the issue that some small business owners use their family home as security for business loans.

As is noted in Government information, the insolvency laws may offer business owners 'more opportunities to restructure their debt, continue trading while insolvent, and avoid foreclosure of their family home'.

Our members have been a key creditor group in some well-publicised insolvencies in Australia, including and especially in 2020 which has seen unprecedented extensions to the liability-free period of Administrators under Part 5.3A of the *Corporations Act*, often leaving landlords without any rent and any right to deal with property for long periods – zero control and zero rights in a period where landlords are already bearing the burden.

Our review of the Draft Regulation and experience tells us that the regime can easily be gamed by small businesses to simply get out of or unilaterally modify their existing lease obligations which were otherwise freely negotiated by fully informed commercial parties.

We are concerned that Treasury may not fully appreciate this, including how this (for example) relates to what we believe to be inadequate definitions of "admissible debt or claim" which would be subject to a restructuring plan and also "liabilities" in connection with the $1 million threshold eligibility test.

This also comes at a time under the Code of Conduct, announced by the Prime Minister on 7 April 2020 and regulated by each State and Territory, that our industry has provided nearly $2 billion in rental assistance to SMEs, to 'share the risk' of the then 'hibernation strategy' and movement and retailer trading restrictions.

Under the Code, the property rights of landlords have been ameliorated to such an extent that the effect is akin to those rights having been extinguished.

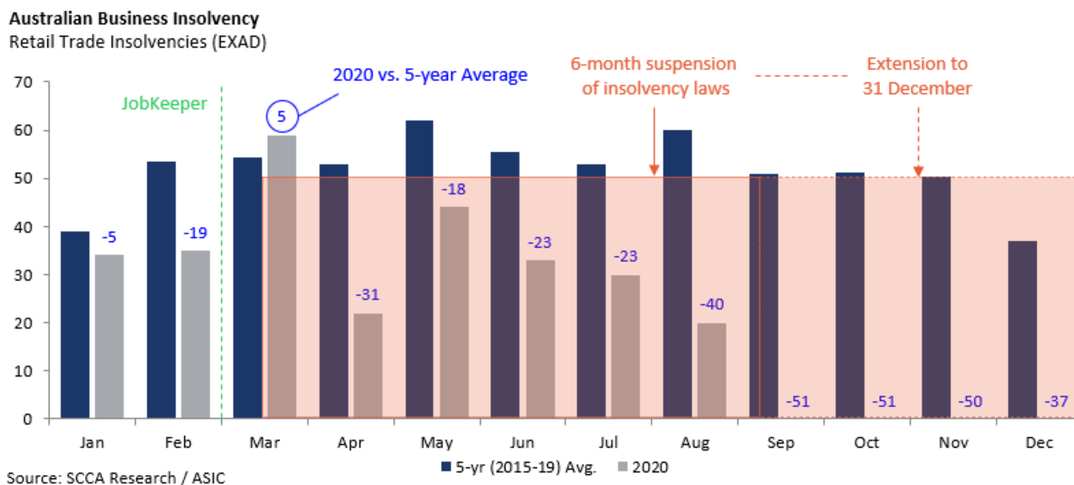
Shopping centre owners have, like the temporary loosening of insolvency laws, been a strong part of the 'relief' effort for small retailers including keeping otherwise healthy businesses from going into liquidation.

It is greatly concerning that while having been part of the relief effort, shopping centre owners stand to be severely adversely impacted by these reforms.

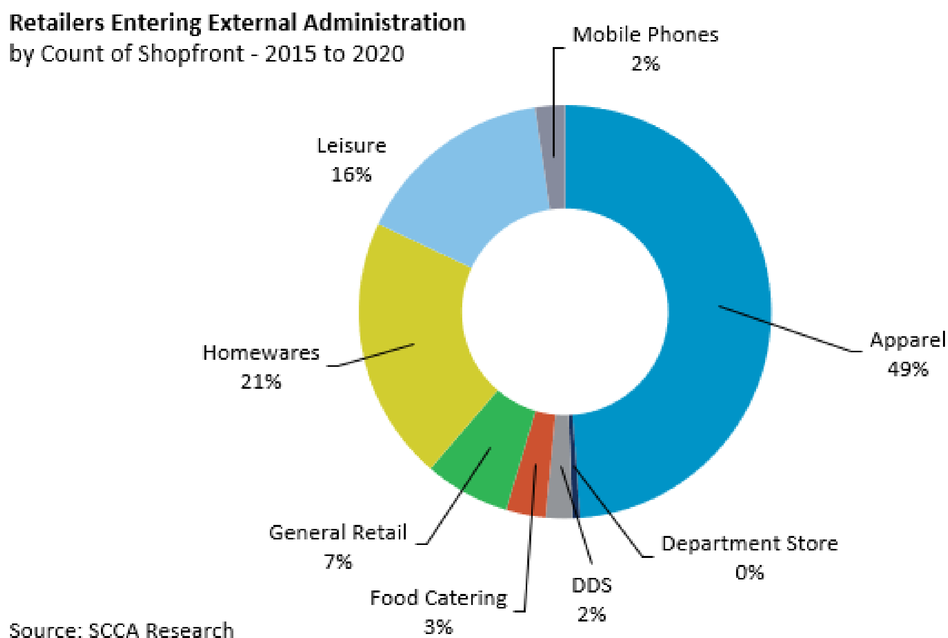
We are also mindful of the unintended consequences when looking at the impact of the temporary suspension or 'loosening' of insolvency laws announced in March 2020, which include providing temporary relief for company directors from personal liability for trading while insolvent and a temporary increase in the threshold for which creditors can issue a statutory demand, is due to expire at the end-of-December 2020. This highlights that a significant number of small retail business insolvencies may be imminent.

The below compares the five-year average (2014-2019) to 2020 data for *Retail Trade* businesses, using insolvency data from ASIC.

Adding the variance to the five-year average between January and September this year, to the five-year average for September to December, results in what could be described as a 'shortfall' of almost 350 retail trade insolvencies for 2020. It could be fair to assume that these businesses, or some of these businesses, will start to fail over the coming months as the changes to JobKeeper permeate the market.



We also track 'retail failures' and are thus mindful of the impact across relevant categories in light of the impacts of COVID-19 including government movement and retailer trading restrictions, noting the current five-year average below:



We are pleased to provide the following comments and recommended amendments, generally in order of priority and referenced for ease of reading:

Regulation	Issues and comment
5.3B.01 (Definitions), 23 (Acceptance of restructuring plan), 26 (Parties to restructuring plan) & 27 (Effect of restructuring plan)	***Issue:*** The definition of "*admissible debt or claim*" is materially disadvantageous to landlords with leases that remain on foot. As a body of unsecured creditors, landlords are likely to have the greatest **present or future certain debt** (i.e. *not* contingent claims). The Courts of Australia and England have made it clear that a landlord's right to receive rent is not a contingent claim. In *Lam Soon Australia Pty Ltd v Molit (No. 55) Pty Ltd* [1996] 70 FCR 34, the court stated: "To suggest that because a contract might be, but has not yet been, repudiated means that an existing contractual obligation to pay money in the future should be treated as giving rise not even to a contingent claim but to a claim "which might never arise" seems to us, with respect, simply wrong. It would apply equally, in principle, to a mortgage debt or terms sale. In truth, there is in each case an existing right; in each case it does not follow, because the right will bear fruit in the future when money is required to be paid, and may be defeasible in certain events, that it is not a claim which has arisen. A question may arise as to the valuation of the claim: in the case of a winding-up that question will be answered by reference to s 554A; in the case of a deed of company arrangement, it may be answered by reference to the terms of the deed." (see also *Foots v Southern Cross Mine Management Pty Ltd [2007] HCA 56* and the UK case of *Re Sutherland, dec'd AC 235*, both of which discuss the distinction between future and contingent claims) Specifically, a claim to rent under a lease is certain and will arise on given dates and is not contingent. Whereas a claim against, for example, a guarantor of a tenant, may never arise and is therefore contingent. Therefore, landlords are overly exposed to restructuring plans which seek to materially alter their contractual right to receive future rent in accordance with a lease. In circumstances where the company incurs debt in the future to creditors who did not have future debt claims at the time of the effectuation of the restructuring plan, those creditors gain an immense advantage at the expense of landlords. For example, assume the debtor company has a supply contract with a widget selling company which sells widgets at $1 per piece. In this circumstance, the liability arises on the delivery of the widgets. Therefore, under a new order post the relevant date, the widget selling company still gets to charge $1 (even under the pre-existing contract), while the landlord's claim to rent is potentially severely compromised. ***Submission 1:*** The definition should make clear that future rent and other future occupancy costs under an existing lease are not captured by the regime. They should be expressly excluded from what is an *admissible debt or claim* under the Bill and the Regulations. ***Submission 2:*** In addition, the restructuring practitioner should be required to consult and reach agreement with landlords. Any claim for future rent under a lease should not be able to be compromised without the agreement of the landlord or where the landlord otherwise notifies its acceptance of the restructuring plan.

	In addition to a change to the definition as per Submission 1, Regulation **5.3B.23** should include a criteria for acceptance of any plan requiring a compromise of future debt to be specifically approved by the affected creditor. A further alternative is to draft a specific provision in the legislation to deal with this issue. An equivalent provision to s.444D(3) should also be included in the legislation.
5.3B.04 (Transactions or dealing in the ordinary course of business)	***Issue:*** Sub-regulation (2)(b) has the effect that rent and other occupancy costs cannot be paid by the company during the restructuring period. Part 5.3A of the Corporations Act contains provisions that the Administrator or Company would otherwise be liable under existing insolvency regimes. Landlords should not be required to bear the cost of the restructuring under these proposed Regulations. It is manifestly unfair to continue to burden landlords with the cost of insolvency. ***Submission:*** The regulation should be amended to make rent and other occupancy costs payable during the restructuring period and to expressly preserve a landlord's rights to enforce the terms of a lease where such costs are not paid by the company. Alternatively, but less attractively, the regulation should be amended to expressly state that the company will remain liable for those amounts and where payment for same is does not form part of the restructuring plan, payment in full will be required at the end of the restructuring and that the lessor is not restrained from enforcing its rights in respect of any unpaid amounts.
5.3B.03 (Eligibility criteria for restructuring)	***Issue 1:*** Where related entities are exempted under s.453C(2)(b), the absence of limits on total liabilities of a group of related entities leaves open the prospect that the system may be "gamed". The Regulations as presently drafted allow for a group of entities with a complex business structure and each with debts near the threshold to take advantage of a system which was not designed for this purpose. Consider the example of a chain of stores each of which operates under a different leasing corporate entity, has as part of its structure a company which employs its staff and one which carries the debt for goods obtained. ***Submission:*** the total liabilities of any group of related entities simultaneously in restructuring should be limited. ***Issue 2:*** A similar issue arises in respect to subsidiaries of a large organisation (whether listed or private) or an Australian subsidiary of a significant overseas concern. ***Submission:*** In order to avoid "shuffling" of assets and liabilities within a corporate group, a limit on the asset size of the group should be implemented, much in the same way as the COVID leasing legislation, but with a vastly lower threshold to avoid gaming by large enterprise.

5.3B.13 (Contents of restructuring plan), 14 (Restructuring proposal statement) & 19 (Proposing a restructuring plan to creditors)	***Issue 1:*** It is not apparent that the Company is required to expose to the creditors its financial position and assets. The company is required to *identify the company's property that is to be dealt with*. It does not appear that the company is required to make known to its creditors what other property it may have that may otherwise be divisible amongst its creditors. This encourages a clandestine approach where other insolvency regimes require a company to be open about its financial position. This prevents a creditor from understanding what its proper position may be. Importantly, however, it creates a regimes where non-disclosure may produce sub-optimal outcomes. ***Submission:*** the company should be required to produce a RATA and statement of financial position to creditors or, at least, that is available to creditors as notified by the restructuring practitioner. ***Issue 2:*** **5.3B.13(4)(b)** The time for making payments is limited to 5 years post the day of the plan. This is commercially unrealistic and out of alignment with any court that might consider an instalment order. ***Submission:*** the time should be limited to two years.
5.3B.19 (Proposing a restructuring plan to creditors) & 20 (Creditors may dispute schedule of debts and claims)	***Issue:*** The lack of a requirement for all creditors to be informed at once within a specified time leaves the regime open to manipulation. In addition, it leaves timeframes uncertain, which is particularly problematic when certain transactions may be prohibited (and indeed lead to offences being committed). Uncertain timeframes do not give parties appropriate parameters within which to assess commercial impacts and outcomes. Certainty of timeframes allows creditors to understand their obligations and rights under both of these Regulations. ***Submission:*** Restructuring practitioners should be required to provide notice to all creditors within a specific time. Alternatively, the restructuring practitioner must be required to provide notice within a specified time to all creditors who will have continuing contracts (e.g. landlords, hirers of equipment etc) with the company post the restructuring.
5.3B.23 (Acceptance of restructuring plan)	***Issue:*** Regulation **5.3B.23** requires a plan to be passed by the majority in value of creditors "*…known at the time the restructuring began …*". This drafting apparently excludes those creditors who become known during the restructuring. This clearly leaves the regime open to corruption. ***Submission:*** This Regulation should be amended to those creditors known at the time of notification under Regulation 5.3B.19
5.3B.55(4) (Courts may limit rights of secured creditor or owner or lessor)	***Issue:*** Where a company makes a restructuring plan and that plan has not yet terminated, the court should not be provided with powers to prevent a landlord from taking possession of property in response to a breach of lease subsequent to the restructuring. The equitable jurisdiction of the courts with respect to remedies including relief against forfeiture is sufficient to protect the interest of tenant companies. ***Submission:*** Sub-Regulations (4) to (6) should be removed.

5.3B.29(4) (Rights of creditors not included in schedule or debts or claims)	***Issue:*** The lack of time limits add uncertainty to the concept of the restructuring period. (See comments re **5.3B.19 & 20** above) ***Submission*:** The restructuring practitioner should be given a limited time period within which to respond, absent a reasonable excuse that requires more time.
5.3B.29(7)(b) (Rights of creditors not included in schedule or debts or claims)	***Issue:*** This sub-Regulation leaves open a system to be "gamed" by the company or a conspiratorial creditor not disclosing the true value of a debt prior to the proposal being made. This, in turn gives rise to the potential for corruption of the regime and puts creditors to the further inconvenience of having to re-assess position regarding acceptance. ***Submission:*** the company should become ineligible if the addition of the debt or claim exceeds more than 10% of the eligibility criteria threshold (presently $1mil)
5.3B.09 (Restructuring practitioner has qualified privilege)	***Issue:*** Qualified privilege is an important and tightly controlled privilege in Australia. The concept is generally limited to specific relationships. This Regulations as drafted is in no way limited. ***Submission:*** Any qualified privilege should be limited to specific relationships – e.g. commentary about the actions of the company and its directors/members. It should not be a privilege "at large".

We appreciate the opportunity to have previously discussed this issue with Treasury.

We would welcome an opportunity to discuss the issues raised in this submission, and I will contact Treasury to arrange a time.

Please don't hesitate to contact me if required.

Yours sincerely,

Angus Nardi

Executive Director