



Australian Government
The Treasury

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Increasing the Statutory Demand Threshold

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Consultation Process

Request for feedback and comments

Closing date for submissions: 5 March 2021

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The principles outlined in this paper have not received Government approval and are not yet law. As a consequence, this paper is merely a guide as to how the principles might operate.

Increasing the Statutory Demand Threshold

Introduction

Following the commencement of the Insolvency reforms to support small business, the Government is consulting on whether to permanently raise the minimum threshold at which creditors can issue a statutory demand on a company.

A statutory demand is a formal demand for payment of a debt owed by a company, issued pursuant to Part 5.4 of the *Corporations Act 2001* (Corporations Act).

A statutory demand can be issued on a company in relation to a debt that is due and payable and totals at least \$2,000. A company is provided 21 days to respond to a demand being made.

On 25 March 2020, in response to the economic impact of COVID-19, the Government temporarily raised the threshold at which a statutory demand could be issued to \$20,000. It also temporarily increased the timeframe that creditors had to respond to a statutory demand, to six months. The intent of these changes was to lessen the threat of actions that could push otherwise viable businesses into insolvency. These changes expired on 31 December 2020, after which the small business insolvency reforms commenced.

This consultation will focus on issues around the monetary threshold at which a statutory demand can be issued by a creditor. The main question is whether the threshold should remain at \$2,000, or whether it should be increased to some other amount going forward.

Request for submissions

Treasury is seeking written submissions from stakeholders on the appropriateness and impacts of permanently increasing the statutory demand threshold. Submissions may be provided until 5 March 2021.

Discussion questions are included to guide feedback. However, stakeholders are welcome to provide further information and suggestions relevant to the issue.

Questions

Question 1: Should the threshold at which a statutory demand can be issued on a company be increased?

Question 2: If the threshold is increased, to what amount should it be increased and why?

Question 3: If the threshold is increased, when should this change come into effect?

Question 4: What will be the impacts of increasing the threshold?

What is a statutory demand?

A statutory demand is a creditor's formal, written request under section 459E of the Corporations Act requiring a company to pay a debt that is due and payable.

The central function of a statutory demand is to establish proof of a company's inability to pay its debts. It does so by creating a rebuttable statutory presumption of insolvency where a company fails to respond to a demand that has been served upon it.

As a result, in practice a company's failure to respond to a demand within the specified time is a common way for a company to enter liquidation, as the affected creditor can then use this presumption to apply to the court to have the company wound up.

It is an abuse of process to use statutory demands for an improper purpose. It has been held by the courts that it is an improper purpose to use statutory demands as a debt recovery tool to coerce someone into paying a disputed debt.

A statutory demand which has been issued as an abuse of process is liable to be set aside. The abuse of process rule reinforces the importance of determining whether any grounds for dispute exist prior to issuing a statutory demand.

Context of consultation

The *Corporate Law Reform Bill 1992* introduced into the national law a requirement that a statutory demand must be for a debt of, or debts totalling, at least the statutory minimum. The statutory minimum was defined to be \$2,000, unless another figure is prescribed.¹ A similar definition was subsequently included in the Corporations Act when the single national law began. Excluding the temporary increase in response to COVID-19, the threshold has not been increased since, through indexation or otherwise.

On 24 September 2020, the Treasurer announced the insolvency reforms to support small business. These changes, which commenced on 1 January 2021, constitute the most significant reforms to Australia's insolvency framework in almost 30 years. The reforms provide Australian small businesses the opportunity to quickly restructure their debts so that they can survive the economic impact of COVID-19. Where restructure is not possible, the reforms allow businesses to be able to wind up faster, enabling greater returns for creditors and employees.

Upon the announcement of the small business insolvency reforms, a factsheet was provided with the Treasurer's media release, which included an announcement that consultation would be undertaken on the appropriateness of permanently raising the minimum threshold at which creditors can issue a statutory demand on a company.

Issues associated with the statutory demand threshold

The Government is aware of a range of issues that have been previously raised in relation to the statutory demand threshold.

Change to the value of money (inflation)

The statutory minimum threshold has decreased in real terms, not having been increased to keep up with inflation. According to the RBA's inflation calculator, a basket of goods valued at \$2,000 in 1992 would be worth \$3,878 in 2020.

While indexing the threshold may address the changes in the real value of the threshold over time, it also carries its own risks. An indexed amount may lead to confusion about what the actual threshold is for a given year and would require information providers to regularly update information. This could create confusion in the market place if parties are relying on out of date information.

¹ The demand process that existed under previous companies legislation is not outlined in this paper, which focuses on the more recent history of statutory demands.

Commercial costs of issuing and defending a demand

While \$2,000 is the legal minimum statutory threshold, some have noted that in practice it may not make sense commercially for a creditor to issue a statutory demand at or near the minimum amount. This is due to the cost involved with drafting and issuing the demand, and possible costs associated with contesting the statutory demand in court if it is disputed by the recipient company.

A statutory demand may also unnecessarily push a company into liquidation, where that company has long term viability and has a chance at a successful restructure. Other than paying or otherwise coming to an agreement with the creditor, the debtor company must apply to the court to have the statutory demand set aside. This will often be a costly process for that business, particularly if they are already in financial distress, which is likely to be common.

Alignment with personal bankruptcy threshold

Until 2010, there was alignment between the threshold for issuing a corporate statutory demand on a company and the threshold for initiating bankruptcy proceedings against an individual debtor through issuing a bankruptcy notice. In 2010, the threshold for issuing a bankruptcy notice was raised from \$2,000 to \$5,000. This threshold was increased again, to \$10,000, on 1 January 2021.

As part of the Government's temporary changes in response to the Coronavirus, the threshold for issuing a demand on both companies and individuals rose to \$20,000. This temporarily brought the thresholds back into alignment, until the temporary changes expired on 31 December 2020.

Harmony between the thresholds can provide desirable consistency between the two different regimes, supporting individuals who run small businesses that need to engage with both regimes where their business is in financial distress.

But there may also be reasons for the difference in thresholds. If an individual is made bankrupt, the personal implications may be more significant than in the corporate context. If a statutory demand forces a company into liquidation the directors of the company may benefit from limited liability, protecting their personal assets. However, in practice a significant number of small business owners have given personal guarantees secured by personal assets (such as their primary residence) in order to obtain financing for their company's liabilities.

Impacts on creditors and debtor companies

Increasing the minimum threshold at which creditors can issue a statutory demand will reduce the ability of some creditors to take action against debtor companies.

As noted above, commercial constraints may make issuing a statutory demand at a lower monetary threshold impractical in many circumstances. On the other hand, reducing the ability of creditors to take action may lead to unintended consequences for companies in financial distress. For example, creditors may decide to manage their risk of non-payment through dealing with the company on less generous terms, such as higher interest rates on loans, a shorter payment period or by requiring cash on delivery.