

EXPLANATORY STATEMENT

Issued by authority of the Treasurer

Corporations Act 2001

Corporations (Fees) Act 2001

Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020

Section 1364 of the *Corporations Act 2001* (the Corporations Act) provides that the Governor-General may make regulations prescribing matters required or permitted by the Corporations Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Corporations Act. Section 8 of the *Corporations (Fees) Act 2001* (the Fees Act) provides that the Governor-General may make regulations for the purposes of sections 5 and 6 of the Fees Act which allow fees to be prescribed.

The purpose of the *Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020* (the Regulations) is to amend the *Corporations Regulations 2001* (the Corporations Regulations) and the *Corporations (Fees) Regulations 2001* (the Fees Regulations) to enable the new debt restructuring and simplified liquidation regimes established by the *Corporations Amendment (Corporate Insolvency Reforms) Act 2020* (the Insolvency Reforms Act), including modification of certain fees. The Regulations also make further consequential amendments to the Corporations Regulations that are required as a result of the Insolvency Reforms Act.

The economic consequences of the Coronavirus known as COVID-19 highlight the need for a system of external administration that can accommodate the needs of small businesses. In these situations, complex, lengthy and rigid procedures can be unsuitable. In response to these challenges, the Australian Government announced a package of reforms to the corporate insolvency framework, including major changes to accommodate eligible small businesses. The additions to the framework are designed to meet the needs of small businesses by reducing the complexity and costs of insolvency processes.

The framework for the reforms is established through the Insolvency Reforms Act. The framework provides for a formal debt restructuring process for eligible companies, extended temporary relief for eligible companies intending to undertake a formal debt restructuring process, a simplified liquidation process for eligible companies in a creditors' voluntary winding up, refinements to the requirements for registration as a liquidator, and greater use of electronic documents and electronic signatures in an external administration.

The Regulations amend the Corporations Regulations to enable the operation of the new external administration processes including by specifying:

- certain eligibility and other requirements for entry into the debt restructuring process and the simplified liquidation process;
- features of the new insolvency processes, such as circumstances where a liquidator or restructuring practitioner must provide a report to ASIC;

- how a company exits the debt restructuring process and the simplified liquidation, including circumstances in which the debt restructuring process ends, circumstances where a company ceases to be eligible for the simplified liquidation process, and transitional arrangements; and
- requirements for a debt restructuring plan, including proposing, making, varying and terminating a restructuring plan.

The Regulations also make amendments to the Fees Regulations to temporarily remove the fee payable to ASIC for the registration of a liquidator, and to provide a fee for a chargeable matter that occurs under the debt restructuring process.

Details of the Regulations are set out in [Attachment A](#).

A Statement of Compatibility with Human Rights, in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*, is at [Attachment B](#).

A Regulation Impact Statement is set out in [Attachment C](#) (OBPR Ref: 25694).

The Corporations Act specifies no conditions that need to be satisfied before the power to make the Regulations may be exercised.

Public consultation was undertaken on the Regulations between 17 and 24 November 2020. Submissions were received from various industry participants and industry bodies. Modifications were made to the Regulations in response to the feedback received.

The Regulations are a legislative instrument for the purposes of the *Legislation Act 2003*.

The Regulations commence as follows:

- Schedule 1 commences on the day after the Regulations are registered or the day on which Schedule 1 to the Insolvency Reforms Act commences, whichever occurs later;
- Schedule 2 commences on the day after the Regulations are registered or the day on which Schedule 2 to the Insolvency Reforms Act commences, whichever occurs later;
- Schedule 3 commences on the day after the Regulations are registered or the day on which Schedule 3 to the Insolvency Reforms Act commences, whichever occurs later;
- Schedule 4 commences on the day after the Regulations are registered or the day on which Schedule 4 to the Insolvency Reforms Act commences, whichever occurs later; and
- Part 1 of Schedule 5 commences on 1 January 2021 and Part 2 of Schedule 5 commences on 1 July 2022.

ATTACHMENT A

Details of the *Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020*

Section 1 – Name of the Regulations

Section 1 provides that the name of the Regulations is the *Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020* (the Regulations).

Section 2 – Commencement

Section 2 provides that sections 1 to 4 of the Regulations commence on the day after the Regulations are registered.

Section 2 also provides that the Schedules to the Regulations commence as follows:

- Schedule 1 to the Regulations commences on the day after this instrument is registered or the day on which Schedule 1 to the *Corporations Amendment (Corporate Insolvency Reforms) Act 2020* (the Insolvency Reforms Act) commences, whichever occurs later;
- Schedule 2 to the Regulations commences on the day after this instrument is registered or the day on which Schedule 2 to the Insolvency Reforms Act commences, whichever occurs later;
- Schedule 3 to the Regulations commences on the day after this instrument is registered or the day on which Schedule 3 to the Insolvency Reforms Act commences, whichever occurs later;
- Schedule 4 to the Regulations commences on the day after this instrument is registered or the day on which Schedule 4 to the Insolvency Reforms Act commences, whichever occurs later; and
- Part 1 of Schedule 5 to the Regulations commences on 1 January 2021 and Part 2 of Schedule 5 to the Regulations commences on 1 July 2022.

Section 3 – Authority

Section 3 provides that the Regulations are made under the *Corporations Act 2001* (the Corporations Act) and the *Corporations (Fees) Act 2001*.

Section 4 – Schedules

Section 4 provides that each instrument that is specified in the Schedules to the Regulations will be amended or repealed as set out in the applicable items in the Schedule concerned, and any other item in the Schedules to the Regulations has effect according to its terms.

Schedule 1 – Amendments relating to debt restructuring

The *Corporations Amendment (Corporate Insolvency Reforms) Act 2020* (the Insolvency Reforms Act) establishes a new formal debt restructuring process for incorporated small businesses. The newly established process enables eligible, financially distressed but potentially viable firms to restructure their existing debts.

Schedule 1 to the Regulations inserts Part 3B in the *Corporations Regulations 2001* (the Corporations Regulations) to provide for the operation of the new formal debt restructuring process.

The debt restructuring process allows an eligible company to restructure their debts and maximise their opportunity for survival. The debt restructuring process allows a company director to retain control of their business, and its property and affairs, while developing a plan to restructure the business' debt with the assistance of a small business restructuring practitioner.

The restructuring process covers the period during which a plan is being developed by the company director(s), following the appointment of a small business restructuring practitioner. The *restructuring process ends* once creditors vote to accept or reject the plan. If a plan is accepted, the company is then *subject to the restructuring plan*. A small business restructuring practitioner is appointed to administer the plan.

The restructuring plan sets out an approach for a company under financial distress to repay its existing debts. During the period that the plan is in place:

- *debts covered by the restructuring plan* will be paid to creditors in accordance with the terms of the plan, until such time as all of the company's obligations under the plan are fulfilled (the plan comes to an end) or the plan is terminated for any other reason; and
- the company can continue to trade (restrictions imposed during the restructuring process no longer apply) – the company is responsible for paying all debts *not covered by the plan* as and when they fall due.

The requirements relating to the debt restructuring plan are prescribed in Schedule 1 to the Regulations.

Legislative references in this Schedule are references to Schedule 1 to the Regulations unless otherwise specified.

Entering the debt restructuring process

Eligibility for the debt restructuring process

Section 453C of the Corporations Act specifies the eligibility criteria that a company must meet to enter into the formal debt restructuring process. The provision provides that a company will be eligible for restructuring where:

- the regulations prescribe a test for eligibility based on the liabilities of the company and the test has been satisfied;

- no director of the company (or any former director who left the company within the last 12 months) has been a director of another company that has been under restructuring or has been the subject of a simplified liquidation process; and
- the company has not been under restructuring or been the subject of a simplified liquidation process.

Section 453C also provides that the Regulations may prescribe exemptions to the prohibition on having previously been engaged in a simplified liquidation or restructuring process.

Liabilities test of the company

Section 453C of the Corporations Act empowers the Corporations Regulations to prescribe a test for eligibility based on the liabilities of the company.

The Regulations prescribe that a company is eligible to enter the restructuring process if the total liabilities of the company on the day that restructuring begins do not exceed \$1 million. The meaning of liabilities includes any liability to pay admissible debts or claims. *[Schedule 1, item 1, regulations 5.3B.03(1) and (5)]*

Previous use more than seven years ago

The eligibility criteria for restructuring in section 453C of the Corporations Act requires that, subject to exceptions prescribed in the regulations, restructuring cannot be used in either of the following scenarios:

- where a director of the company (or any former director who left the company within the last 12 months) has been a director of another company that has been under restructuring or has been the subject of a simplified liquidation process;
- the company has been under restructuring or the subject of a simplified liquidation process.

In part, these rules are designed to target illegal phoenixing and other high risk behaviours.

Phoenix activity can encompass both legitimate business rescue activities and the use of serial deliberate insolvency as a business model to avoid paying company debts. While the scale of illegal phoenix activity ranges from the opportunistic to the systemic, a common characteristic is the stripping and transfer of assets from a company to another entity. Such transactions are carried out by a company's directors or other controlling minds with the intention of defeating the interests of the first company's creditors in that company's assets. Such transactions are also facilitated by others, including unscrupulous pre-insolvency advisers, accountants, lawyers or other business advisers, who advise companies on how to engage in illegal phoenix activity. In many cases a new company is then started to continue with the same or similar business activities without the existing debt.

Some examples of signs that can point to illegal phoenix activity include:

- employees have transferred to a new company;
- company directors have been involved with liquidated entities before;
- requests for payments or contracts to be paid to a new company;
- recent changes to a company's directors including the use of straw or dummy directors;
- assets disposed of prior to liquidation not at market value to related entities or parties.

The rule against previous use of restructuring or simplified liquidation is particularly designed to target the potential indicator of illegal phoenix behaviour where company directors have been involved with liquidated entities before. However, in some circumstances, previous involvement with liquidated entities is not considered a potential indicator of illegal phoenix behaviour. To address these circumstances, the Regulations prescribe circumstances in which the previous use rule in section 453C of the Corporations Act does not apply.

The Regulations prescribe a period of seven years as the period in which the previous use rule applies. The effect is that a director or company is eligible for the formal debt restructuring process where the director or the company previously used either the restructuring process or the simplified liquidation process more than seven years prior to the company seeking to satisfy the eligibility criteria for the restructuring process.
[Schedule 1, item 1, regulations 5.3B.03(2) and (3)]

Previous use by a related body corporate

The Regulations prescribe circumstances where the company seeking to undergo the restructuring process may be exempt from the requirements that neither a director (nor former director) of the company, nor the company itself, has been under restructuring or been the subject of a simplified liquidation process within a seven-year period. This occurs where:

- the other company is a related body corporate of the company seeking to undergo the restructuring process;
- if the other company is, or has been, undergoing restructuring—the restructuring began no more than 20 business days before the beginning of restructuring for the company seeking to undergo the restructuring process; and
- if the other company is, or has been, subject to a simplified liquidation process—the other company began to follow the simplified liquidation process no more than 20 business days before the beginning of restructuring for the company seeking to undergo the restructuring process.

[Schedule 1, item 1, regulation 5.3B.03(4)]

The intention is to allow different companies within a body corporate group to enter into the restructuring process at the same time. This reflects the likelihood that if multiple companies within a corporate group are insolvent or likely to become insolvent, some or all of the companies that comprise the group will need to restructure or liquidate at the same or roughly the same time. In many instances, these related companies will have common directors. The term ‘related body corporate’ includes a company that is a holding company or subsidiary of the other (see sections 9 and 50 of the Corporations Act).

Director’s declaration

The Regulations prescribe that within five business days after the day on which the restructuring of a company begins, or such a longer period as the company’s small business restructuring practitioner allows, the directors must provide the small business restructuring practitioner with a declaration in the approved form (if any).

[Schedule 1, item 1, regulation 5.3B.49(1)]

The period of five business days could, for example, be used by directors to seek assistance from the small business restructuring practitioner to make the declaration.

The declaration must state:

- whether or not, in the directors’ opinion, there are reasonable grounds to believe that the company has entered into a transaction that would be voidable under section 588FE of the Corporations Act, excluding unfair preferences, in the event that the company were wound up; and
- whether or not, in the directors’ opinion, there are reasonable grounds to believe that the eligibility criteria for restructuring were met in relation to the company at the time the restructuring began, and set out the reasons for that opinion.

[Schedule 1, item 1, regulations 5.3B.49(2)(b) to (c)]

The declaration must be signed by each director of the company. *[Schedule 1, item 1, regulation 5.3B.49(3)]*

This declaration is intended to safeguard against potential illicit behaviour in the lead up to restructuring. For example, it would prevent company directors from transferring assets out of the company for creditor defeating purposes. A failure by a director to provide a declaration is an offence under section 1311(1) of the Corporations Act. In addition, if a director provides false or misleading information in the declaration, the director may be subject to civil or criminal penalties under section 1308 of the Corporations Act. These existing penalties within the Corporations Act penalties framework provide an appropriate level of deterrence against directors providing false or misleading information to the small business restructuring practitioner in order to enter into the restructuring process.

The directors' declaration must be made in the form approved by ASIC, if any, and lodged with ASIC. *[Schedule 1, item 1, regulations 5.3B.49(2)(a) and 5.3B.65]*

Features of the restructuring process

The company entering into a transaction or dealing affecting the property of the company

Generally, where the company is under restructuring, the company or the directors on behalf of the company, must not purport to enter into a transaction or dealing affecting the property of the company. A director who breaches this requirement commits an offence, the penalty for which is up to six months' imprisonment (see sections 453L(1) and 1311(1) and Schedule 3 to the Corporations Act).

However, this prohibition does not apply if:

- entering into the transaction or dealing was in the ordinary course of the company's business;
- the small business restructuring practitioner has consented to the transaction or dealing and, if any conditions are imposed on that consent, those conditions are met; or
- the transaction or dealing was entered into under an order of the Court.

Section 453L(4) of the Corporations Act specifies that the Corporations Regulations may prescribe circumstances in which entering into a transaction or dealing is, or is not, to be treated as 'in the ordinary course of business' for a company. The Regulations prescribe the following circumstances in which entering into a transaction or dealing by a company is not to be treated as in the ordinary course of the company's business:

- the transaction or dealing is for the purpose of satisfying an admissible debt or claim;
- the transaction or dealing is for the transfer or sale of the whole or part of the business; and
- the transaction or dealing is for the payment of a dividend.

[Schedule 1, item 1, regulation 5.3B.04]

Where a company wishes to enter into a transaction or dealing that is outside the ordinary course of business, the board of the company may request consent from the small business restructuring practitioner as per section 453L(2) of the Corporations Act. *[Schedule 1, item 1, regulation 5.3B.05(1)]*

Consent must be given in writing or, if conditions are met, orally. *[Schedule 1, item 1, regulation 5.3B.05(2)]*

If the restructuring practitioner gives the consent in writing, the consent must specify any conditions imposed on the consent. *[Schedule 1, item 1, regulation 5.3B.05(3)]*

The small business restructuring practitioner may provide consent orally if the practitioner is satisfied that the delay caused by giving consent in writing would not be in the best interests of the company's creditors. The restructuring practitioner must, within two business days after giving this consent, make a written record of the consent and any conditions and provide a copy to the company. *[Schedule 1, item 1, regulations 5.3B.05(2)(b) and (4)]*

Consent by the small business restructuring practitioner to transactions or dealings outside of the ordinary course of business is subject to section 453L(6) of the Corporations Act. This section provides that consent can only be given where the practitioner believes on reasonable grounds that it would be in the interests of the company's creditors to enter into the transaction or dealing.

The small business restructuring practitioner must keep a record of the consent for five years. Failure to keep a record for the required period is an offence under section 1311(1) of the Corporations Act. *[Schedule 1, item 1, regulation 5.3B.05(5)]*

Rights not subject to the stay on enforcing rights triggered by restructuring

Section 454N(1) of the Corporations Act provides, generally, that a right cannot be enforced against a company for the reason that the company has come or is under restructuring if the right arises for that reason by express provision of a contract, agreement or arrangement.

Under section 454N(5) of the Corporations Act, the Regulations prescribe kinds of contracts, agreements or arrangements in relation to which the stay does not apply. *[Schedule 1, item 1, regulation 5.3B.12]*

The kinds of contracts, agreements or arrangements prescribed in the Regulations mirror those prescribed in relation to other forms of external administration: (see section 451E and regulation 5.3A.50); arrangement or reconstruction (see section 415D and regulation 5.1.50); and where a managing controller has been appointed (see section 434J and regulation 5.2.50).

This has the effect that the stay on proceedings in section 454N(1) of the Corporations Act does not apply to a contract, agreement or arrangement of the kind prescribed in regulation 5.3A.50(2). These are:

- an agreement (within the meaning of the *Convention* defined in section 3 of the *International Interests in Mobile Equipment (Cape Town Convention) Act 2013*);
- a contract, agreement or arrangement that is a licence, permit or approval issued by:
 - the Commonwealth, a State or a Territory; or
 - an authority of the Commonwealth or of a State or a Territory; or
 - a local governing body established by or under a law of a State or Territory;
- a contract, agreement or arrangement relating to Australia's national security, border protection or defence capability;
- a contract, agreement or arrangement for the supply of goods or services to a public hospital or a public health service;
- a contract, agreement or arrangement for the supply of goods or services by or on behalf of a public hospital or a public health service;
- a contract, agreement or arrangement for the supply of essential or critical goods or services to, or the carrying out of essential or critical works for:
 - the Commonwealth, a State or a Territory; or
 - an authority of the Commonwealth or of a State or a Territory; or
 - a local governing body established by or under a law of a State or Territory; or
 - the public on behalf of one of these entities;
- a contract, agreement or arrangement that is, or is directly connected with, a derivative;
- a contract, agreement or arrangement that is, or is directly connected with, a securities financing transaction;
- a contract, agreement or arrangement for the underwriting of an issue, or sale, of securities, financial products, bonds, promissory notes, or syndicated loans;
- a contract, agreement or arrangement under which a party is or may be liable to subscribe for, or to procure subscribers for, securities, financial products, bonds, promissory notes, or syndicated loans;
- a contract, agreement or arrangement that is, or governs, securities, financial products, bonds, promissory notes, or syndicated loans;

- a contract, agreement or arrangement under which securities are offered, or may be offered, under a rights issue;
- a contract, agreement or arrangement for the sale of all or part of a business, including by way of the sale of securities or financial products;
- a contract, agreement or arrangement for the issue of an instrument that:
 - is a security, financial product, bond, promissory note, or syndicated loan; and
 - belongs to a class of such instruments, each of which is fungible, and the first of which was issued before 1 July 2018;
- a contract, agreement or arrangement that is, or is directly connected with, a margin lending facility (within the meaning of Chapter 7 of the Corporations Act – relating to financial services and markets);
- a contract, agreement or arrangement that is:
 - a covered bond (within the meaning of the *Banking Act 1959*); or
 - for issuing such a bond; or
 - directly connected with such a bond or the issuing of such a bond;
- a contract, agreement or arrangement providing for the management of financial investments;
- a contract, agreement or arrangement that involves a special purpose vehicle, and that provides for securitisation or a public-private partnership;
- a contract, agreement or arrangement that involves a special purpose vehicle, and that provides for a project finance arrangement under which:
 - a financial accommodation is to be repaid or otherwise discharged primarily from the project’s cash flow; and
 - all or substantially all of the project’s assets, rights and interests are to be held as security for the financial accommodation;
- a contract, agreement or arrangement for the keeping in escrow of:
 - code, or passwords, for computer software; or
 - material directly associated with such code or passwords;
- a contract, agreement or arrangement for the commercial charter of a ship if:
 - the ship is not an Australian ship (within the meaning of the *Shipping Registration Act 1981*); and

- the charter is by an Australian national (within the meaning of that Act) for the purposes of exporting goods from Australia, or from an external Territory, to another country;
- a contract, agreement or arrangement under which the priority of security interests in particular property is changed or can change;
- a contract, agreement or arrangement that is a flawed asset arrangement;
- a contract, agreement or arrangement that is, or is directly connected with, a factoring arrangement (within the meaning of the *ASIC Corporations (Factoring Arrangements) Instrument 2017/794*);
- a contract, agreement or arrangement that is the operating rules (other than the listing rules) of a financial market;
- a contract, agreement or arrangement that is the operating rules of a clearing and settlement facility;
- a contract, agreement or arrangement that confers rights on the operator of a financial market, or the operator of a clearing and settlement facility, in relation to the operation of the market or facility;
- a contract, agreement or arrangement of which the parties include the Reserve Bank of Australia and the operator of a clearing and settlement facility;
- a contract, agreement or arrangement under which participants (within the meaning of Chapter 7 of the Corporations Act – relating to financial services and markets) in a clearing and settlement facility may settle obligations on behalf of other participants (within the meaning of that Chapter) in the facility;
- a legally enforceable arrangement referred to in paragraph 9(1)(b) of the *Payment Systems and Netting Act 1998* that supports an approved RTGS system (within the meaning of that Act);
- an approved netting arrangement (within the meaning of the *Payment Systems and Netting Act 1998*);
- a contract, agreement or arrangement that confers rights on:
 - the operator of an approved RTGS system (within the meaning of the *Payment Systems and Netting Act 1998*); or
 - the coordinator of an approved netting arrangement (within the meaning of that Act);

in relation to the operation of that system or netting arrangement;

- a contract, agreement or arrangement under which the parties to an arrangement that is a legally enforceable arrangement referred to in paragraph 9(1)(b) of the *Payment Systems and Netting Act 1998* or an

approved netting arrangement within the meaning of that Act (the main arrangement) may settle obligations on behalf of other parties to the main arrangement;

- a close-out netting contract (within the meaning of the *Payment Systems and Netting Act 1998*);
- a contract, agreement or arrangement under which security is given over financial property (within the meaning of the *Payment Systems and Netting Act 1998*) in respect of eligible obligations (within the meaning of that Act) of a party to a contract that is a close-out netting contract (within the meaning of the *Payment Systems and Netting Act 1998*);
- a netting market (within the meaning of the *Payment Systems and Netting Act 1998*);
- a market netting contract (within the meaning of the *Payment Systems and Netting Act 1998*);
- a contract, agreement or arrangement under which security is given, in accordance with a market netting contract (within the meaning of the *Payment Systems and Netting Act 1998*) in respect of obligations of a party to the market netting contract;
- a contract, agreement or arrangement that is an outsourcing arrangement for the purposes of Prudential Standard CPS *Outsourcing* or Prudential Standard SPS 231 *Outsourcing*;
- a contract, agreement or arrangement entered into or renewed on or after 1 July 2018, but before 1 July 2023, as a result of either of the following:
 - the novation of, or the assignment of one or more rights under, a contract, agreement or arrangement entered into before 1 July 2018;
 - a variation of a contract, agreement or arrangement entered into before 1 July 2018;
- a contract, agreement or arrangement entered into on or after 1 July 2018, but before 1 July 2023, for the provision of any of the following kinds of work, goods or services for a particular project:
 - building work (within the meaning of the *Building and Construction Industry (Improving Productivity) Act 2016*);
 - work to be carried out anywhere in Australia that, if carried out in New South Wales, would be covered by paragraph 5(1)(d) or (f) of the *Building and Construction Industry Security of Payment Act 1999* (NSW) and not be excluded by subsection 5(2) of that Act;
 - goods or services to be provided anywhere in Australia that, if provided in New South Wales, would be related goods and services

(within the meaning of the *Building and Construction Industry Security of Payment Act 1999* (NSW));

if the total payments under all contracts, agreements or arrangements for the project for work, goods or services of those kinds is at least \$1 billion;

- a contract, agreement or arrangement that:
 - is entered into to enable the satisfactory completion of a contract, agreement or arrangement covered above (relating to kinds of work, goods or services within the meaning of the *Building and Construction Industry Security of Payment Act 1999* (NSW)); and
 - is for the provision of a kind of work, goods or services covered by that paragraph.

Small business restructuring practitioner for company under restructuring

Under section 453B of the Corporations Act, a company may appoint a small business restructuring practitioner if it meets the requirements specified in that section.

Within one business day after being appointed, the small business restructuring practitioner must lodge a notice of appointment, in the prescribed form (if any) and in accordance with regulation 5.6.75(4), with ASIC. *[Schedule 1, item 1, regulation 5.3B.50(1)]*

The restructuring practitioner must also, within one business day after being appointed, give the following information to as many of the company's creditors as reasonably practicable:

- the fact that the company has appointed the restructuring practitioner;
- information about the company including the company's name, any trading name, and Australian Company Number (ACN);
- the name and contact details of the restructuring practitioner;
- the date the restructuring practitioner was appointed;
- the restructuring process and the process for making a restructuring plan, including the proposal period, duration of acceptance period and how affected creditors may verify or dispute the creditor's admissible debt or claims;
- how to obtain further information about the restructuring process and the making of a restructuring plan; and
- the right of creditors to request information, reports and documents.

[Schedule 1, item 1, regulation 5.3B.50(2)]

Section 453E(2) of the Corporations Act provides that the Corporations Regulations may provide for and in relation to the functions, duties and powers of the small business restructuring practitioner for a company under restructuring. *[Schedule 1, item 1, regulation 5.3B.07]*

If the appointment of a small business restructuring practitioner for a company terminates for any reason other than their death, the restructuring practitioner must lodge a notice, in the prescribed form (if any), with ASIC within two business days after the day on which the appointment terminated. *[Schedule 1, item 1, regulation 5.3B.51(b)]*

If the appointment of a small business restructuring practitioner for a company terminates because of the death of the practitioner, the company must lodge a notice, in the prescribed form (if any), with ASIC within two business days after the day on which the appointment terminated. *[Schedule 1, item 1, regulation 5.3B.51(a)]*

Powers of the small business restructuring practitioner for a company under restructuring

The Regulations prescribe that the small business restructuring practitioner for a company under restructuring has the power to investigate the company's business, property, affairs and financial circumstances for the purposes of:

- preparing a declaration to certify the restructuring plan;
- deciding whether to terminate the restructuring of the company;
- resolving a disagreement relating to a creditor's schedule of debts and claims;
or
- performing or exercising any other function, duty or power as the small business restructuring practitioner for the company.

[Schedule 1, item 1, regulation 5.3B.08]

Qualified privilege for a small business restructuring practitioner for a company under restructuring

The Regulations also specify that a person who is or has been a small business restructuring practitioner for a company under restructuring has qualified privilege in respect of a statement made, orally or in writing, in the course of performing or exercising any of their functions and powers as a small business restructuring practitioner for the company. *[Schedule 1, item 1, regulation 5.3B.10]*

Protection from liability for a small business restructuring practitioner for a company under restructuring

The Regulations also specify that a current or former small business restructuring practitioner appointed for the company is not liable to any person for anything the practitioner has done or omitted to do in good faith and without negligence, in the performance or exercise, or purported performance or exercise, of their functions, powers or duties as small business restructuring practitioner for the company. *[Schedule 1, item 1, regulation 5.3B.11]*

Duties of a replacement restructuring practitioner for the company

Section 456E(1) of the Corporations Act provides that where a vacancy arises in the office of small business restructuring practitioner for the company, a replacement restructuring practitioner can be appointed.

A replacement restructuring practitioner must fulfil certain past requirements concerning the resolution of creditor disputes and lodging outstanding notices. *[Schedule 1, item 1, regulations 5.3B.09]*

Specifically, the replacement restructuring practitioner must:

- resolve any creditor disputes about the schedule of debts and claims that arose either before or at the time of their appointment by issuing a notice specifying whether the practitioner will consider the dispute; and *[Schedule 1, item 1, regulations 5.3B.09(1) and (2)]*
- lodge or provide any outstanding information, reports, documents or notices within two business days after day they are appointed. *[Schedule 1, item 1, regulation 5.3B.09(3)]*

End of the restructuring process

Section 453A of the Corporations Act specifies that the circumstances under which the restructuring process of a company ends are to be prescribed by the Corporations Regulations.

The Regulations prescribe that the restructuring of a company ends if:

- the directors of a company make a declaration in writing that restructuring is to end on a specified day;
- the company fails to propose a restructuring plan within the proposal period;
- the company's proposal to make a restructuring plan lapses;
- the small business restructuring practitioner for the company terminates the restructuring process under section 453J of the Corporations Act;
- the Court orders that the restructuring of the company is to end;
- an administrator, liquidator or provisional liquidator is appointed to the company;
- if the company is a general insurer (within the meaning of the *Insurance Act 1973*)—management of the general insurer vests in a judicial manager of the company appointed by the Federal Court under Part VB of that Act;
- if the company is a life company (within the meaning of the *Life Insurance Act 1995*)—management of the life company vests in a judicial manager of the life company appointed by the Federal Court under Part 8 of that Act; or

- the company makes a restructuring plan.

[Schedule 1, item 1, regulation 5.3B.02(1)]

The directors of a company may declare that the restructuring of the company is to end for any reason. Where the directors of a company under restructuring make a declaration that restructuring is to end, the declaration must be in writing and specify the day on which restructuring is to end. The directors must give a copy of the declaration to the company's small business restructuring practitioner and the company's creditors before the day specified in the declaration. *[Schedule 1, item 1, regulation 5.3B.02(2)]*

Where the small business restructuring practitioner for a company terminates the restructuring process under section 453J of the Corporations Act, the practitioner must give notice of the termination, in writing, to the company and as many of its creditors as reasonably practicable. This notice must include certain information prescribed in the Corporations Regulations. *[Schedule 1, item 1, regulation 5.3B.02(1)(d)]*

The Regulations prescribe that the small business restructuring practitioner's notice of termination must include all of the following information:

- the name and any trading name of the company;
- the ACN of the company;
- the address of the company's registered office;
- any website maintained by or on behalf of the company;
- the company's email address (if any).

[Schedule 1, item 1, regulation 5.3B.06(a)]

The Regulations also prescribe that the following details about the small business restructuring practitioner are to be provided in a notice of termination:

- the small business restructuring practitioner's name;
- the address and telephone number of the principal place where the small business restructuring practitioner practices as a registered liquidator;
- if the restructuring practitioner practises as a registered liquidator as a member of a firm or under a name or style other than their own name—the name of that firm or the name or style under which the practitioner practises; and
- the small business restructuring practitioner's Registered Liquidator Number as specified on the Register of Liquidators.

[Schedule 1, item 1, regulation 5.3B.06(b)]

The Regulations also prescribe that the following information must be provided in a notice of termination:

- the day on which the restructuring of the company began;
- the day on which the notice is given to the company for termination of the restructuring;
- the reason for terminating the restructuring;
- the signature of the small business restructuring practitioner; and
- any other information that the small business restructuring practitioner considers appropriate.

[Schedule 1, item 1, regulations 5.3B.06(c) to (g)]

Debt restructuring plan

Once a small business restructuring practitioner has been appointed to the company, the directors, on behalf of the company, develop a debt restructuring plan. The debt restructuring plan must be proposed to the creditors within 20 business days of starting the restructuring process.

Section 455B of the Corporations Act provides for a range of regulation-making powers to prescribe matters relevant to a restructuring plan.

To establish the legislative framework for debt restructuring plans under new Part 5.3B of the Corporations Act, the Regulations prescribe information relating to:

- proposing a restructuring plan;
- making, varying and terminating a restructuring plan;
- debts and claims in relation to a restructuring plan;
- contributories in relation to a restructuring plan;
- circumstances in which the restructuring plan is void and the consequences if all or part is void;
- circumstances that constitute a contravention of a restructuring plan and the consequences of the contravention;
- the small business restructuring practitioner for a restructuring plan;
- information, reports or other documents in relation to a restructuring plan; and
- powers of the Court in relation to a restructuring plan.

These matters are discussed in further detail below.

Proposing a restructuring plan

Section 455A of the Corporations Act provides that if a company proposes a debt restructuring plan to its creditors, the company is taken to be insolvent. Section 455A further provides that regulations may prescribe the time at which the company is taken to have proposed a restructuring plan.

The Regulations prescribe that the company is taken to have proposed a debt restructuring plan – and is therefore insolvent – on the day the company’s small business restructuring practitioner gives the proposed restructuring plan and associated documentation to affected creditors. *[Schedule 1, item 1, regulation 5.3B.14(2)]*

In this context, an ***affected creditor*** is a creditor who would be a party to the restructuring plan if it were made. Once the plan is made, all creditors who had admissible debts or claims when the plan was made, are affected creditors. *[Schedule 1, item 1, regulation 5.3B.01]*

Section 455B of the Corporations Act provides for a range of regulation-making powers to prescribe matters relevant to a restructuring plan, including how a restructuring plan is proposed to affected creditors. *[Schedule 1, item 1, regulations 5.3B.13]*

The Regulations provide that a company under restructuring proposes a restructuring plan if:

- the company prepares a compliant restructuring plan and a restructuring proposal statement;
- the company executes the restructuring plan during the proposal period;
- the company’s small business restructuring practitioner prepares and signs a certifying declaration in respect of the restructuring plan;
- the restructuring practitioner gives the restructuring plan, restructuring proposal statement and certifying declaration to affected creditors; and
- before the restructuring plan and other documents required by regulation 5.3B.21 are provided to affected creditors, the company has paid employee entitlements that are payable, and given returns, notices, statements, applications or other documents as required by taxation laws (within the meaning of the *Income Tax Assessment Act 1997*).

[Schedule 1, item 1, regulations 5.3B.14, 5.3B.21 and 5.3B.24(a)]

Preparing a restructuring plan

A company under restructuring must prepare a restructuring plan that complies with the requirements of the Corporations Regulations. *[Schedule 1, item 1, regulation 5.3B.15(1)]*

A restructuring plan must:

- be in the approved form (if any);

- identify the company's property that is to be dealt with;
- specify how the property is to be dealt with;
- provide for the remuneration of the small business restructuring practitioner for the plan; and
- specify the date on which the restructuring plan was executed.

[Schedule 1, item 1, regulation 5.3B.15(2)]

The restructuring plan may also:

- authorise the small business restructuring practitioner for the plan to deal with the identified property in a particular way;
- provide for any matter relating to the company's financial affairs; and
- be subject to the occurrence of a specified event that must occur within 10 business days after the day on which affected creditors accept the draft restructuring plan.

[Schedule 1, item 1, regulation 5.3B.15(3)]

The proposed restructuring plan must not provide for the transfer of property (other than money) to a creditor, and the duration of the plan must not exceed three years from when the plan is made. A plan exceeds three years if it provides for the company to make payments under the plan, in respect of an admissible debt or claim, after three years beginning on the day the plan is made. *[Schedule 1, item 1, regulation 5.3B.15(4)]*

In addition to the prescribed contents of a restructuring plan as outlined above, each restructuring plan is taken to include a set of standard terms. *[Schedule 1, item 1, regulation 5.3B.21(a)(ii)]*

These ***restructuring plan standard terms*** are prescribed as follows:

- all admissible debts and claims rank equally;
- if the total amount paid by the company under the plan in respect of those debts or claims is insufficient to meet those debts or claims in full, those debts or claims are paid proportionately;
- a creditor is not entitled to receive, in respect of an admissible debt or claim, more than the amount of the debt or claim;
- the amount of an admissible debt or claim is ascertained as at the time immediately before restructuring began; and
- if a creditor is a secured creditor:
 - if the creditor does not realise the creditor's security interest while the plan is in force, the creditor is taken, for the purposes of working out

the amount payable to the creditor under the plan, to be a creditor only to the extent (if any) by which the amount of the creditor's admissible debt or claim exceeds the value of the creditor's security interest; and

- if the creditor realises the creditor's security interest while the plan is in force, the creditor is taken, for the purposes of working out the amount payable to the creditor under the plan, to be a creditor only to the extent of any balance due to the creditor after deducting the net amount realised.

[Schedule 1, item 1, regulation 5.3B.27(1)]

A restructuring plan is void to the extent that it is inconsistent with any of these standard terms. *[Schedule 1, item 1, regulation 5.3B.27(2)]*

The company must also prepare a **restructuring proposal statement** to accompany the restructuring plan. *[Schedule 1, item 1, regulations 5.3B.01 and 5.3B.16(1)]*

This statement must:

- include a schedule of debts and claims to be covered by the restructuring plan;
- be in the approved form (if any); and
- contain the information required by the form.

[Schedule 1, item 1, regulation 5.3B.16(2)]

A schedule of debts and claims should comprise a list of known debts and claims owed by the company, including the names of creditors and information relating to the creditor's status, such as if they are an excluded creditor.

An **excluded creditor** is a creditor who is the restructuring practitioner for the company, a related creditor of the company, or a related entity of the restructuring practitioner. *[Schedule 1, item 1, regulation 5.3B.01]*

The company finalises the proposed restructuring plan

Once a restructuring plan has been prepared, the company must execute the restructuring plan within the proposal period. The **proposal period** is 20 business days from the day the restructuring process began. *[Schedule 1, item 1, regulations 5.3B.01, 5.3B.14(1)(b) and 5.3B.17(1)]*

Regulation 5.3B.14(1)(b) requires that the company execute the restructuring plan. Section 127 of the Corporations Act provides that a document is executed if it is signed by either two directors, a director and a company secretary, or one director only (if the company has a sole director who is also the sole company secretary).

The company's small business restructuring practitioner may, on application by the company, extend the proposal period by up to 10 business days. The small business restructuring practitioner may only extend the proposal period if they are satisfied on reasonable grounds that it would not be reasonable, in the circumstances, to require

the company to provide a restructuring plan within the proposal period. *[Schedule 1, item 1, regulation 5.3B.17(2)]*

An extension may be reasonable in the circumstances where, for example, an illness or other unforeseeable event significantly impacts the company directors' ability to finalise and execute the proposed plan within the 20 business day proposal period.

The proposal period may not be extended more than once by the small business restructuring practitioner. *[Schedule 1, item 1, regulation 5.3B.17(3)]*

The Court may also extend the proposal period as it considers appropriate, on application by the company. *[Schedule 1, item 1, regulation 5.3B.17(4)]*

The small business restructuring practitioner must, within two business days after the day on which the proposal period is extended, lodge a notice in the prescribed form (if any) and in accordance with regulation 5.6.75(4), with ASIC and give a copy of the notice to as many of the company's creditors as reasonably practicable. *[Schedule 1, item 1, regulation 5.3B.17(5)]*

Small business restructuring practitioner must make a certifying declaration of the proposed restructuring plan

As soon as practicable after the company executes the proposed restructuring plan, the small business restructuring practitioner must make and sign a certifying declaration in relation to the plan. *[Schedule 1, item 1, regulations 5.3B.18(1) and (3)]*

The purpose of the certifying declaration is to provide the affected creditors with an assurance that the proposed restructuring plan contains all relevant information to enable the creditors to make an informed decision whether to accept or reject the proposed restructuring plan. This is similar to the requirement for a debt agreement administrator's certificate contained in the *Bankruptcy Act 1966*.

The certifying declaration must state that the restructuring practitioner believes on reasonable grounds that:

- the company meets the eligibility criteria;
- the company is likely to be able to discharge the obligations created by the restructuring plan as and when they become due and payable; and
- all information required to be set out in the company's restructuring proposal statement has been set out.

[Schedule 1, item 1, regulations 5.3B.18(2)(a) and (b)]

If the restructuring practitioner does not believe on reasonable grounds that the company has met the above criteria, the practitioner must identify which criteria have not been met, as well as the reasons supporting the practitioner's conclusions. *[Schedule 1, item 1, regulation 5.3B.18(2)(c)]*

If an affected creditor is also a related entity of the restructuring practitioner, the certifying declaration must specify the name of the affected creditor and the nature of

the relationship between the affected creditor and the restructuring practitioner. *[Schedule 1, item 1, regulation 5.3B.18(2)(d)]*

If a restructuring practitioner provides false or misleading information, or omits information that would render the certifying declaration materially false or misleading, the practitioner may be subject to civil or criminal penalties under section 1308 of the Corporations Act. These are existing penalties within the Corporations Act penalties framework, and provide an appropriate level of deterrence in relation to the restructuring practitioner's obligation to certify the restructuring plan.

Further to the offences in section 1308 of the Corporations Act for providing false or misleading information, the small business restructuring practitioner must make reasonable inquiries into, and take reasonable steps to verify, the company's business, property, affairs and financial circumstances for the purpose of assessing the accuracy and completeness of the information provided in the company's proposed restructuring plan and restructuring proposal statement. A failure by the practitioner to make these reasonable inquiries and take these reasonable steps when preparing a certifying declaration is an offence of strict liability. The penalty for this offence is 50 penalty units. *[Schedule 1, item 1, regulations 5.3B.18(4) and (5)]*

A strict liability offence is appropriate to provide an incentive for the small business restructuring practitioner to meet their duties, functions and obligations during the restructuring process thus maintaining the integrity of the process.

The restructuring practitioner is required to notify the company of any defect in its restructuring plan or proposal statement. If at any time before the small business restructuring practitioner prepares the certifying declaration for the proposed restructuring plan, the practitioner becomes aware that information contained in the plan or statement is incomplete or inaccurate, and has reasonable grounds to believe this is likely to affect the company's ability to meet its obligations under the plan, the restructuring practitioner must notify the company and provide an opportunity for the company to address their concerns. *[Schedule 1, item 1, regulation 5.3B.19(1)]*

The small business restructuring practitioner commits an offence if they fail to notify the company of this information. The offence is an offence of strict liability and the penalty for the offence is 50 penalty units. *[Schedule 1, item 1, regulation 5.3B.19(2)]*

The strict liability offences enhance the integrity of the certification by the restructuring practitioner of the proposed restructuring plan. The offence is not punishable by imprisonment, and carries a penalty of only 50 penalty units. The penalty is therefore consistent with the Attorney-General's Department's *Guide to Framing Commonwealth Offences, Infringement, Notices and Enforcement Powers* (September 2011 Edition) (the Guide to Framing Commonwealth Offences).

Company must ensure employee entitlements are paid and each tax reporting obligation is substantially complied with

Before the restructuring plan is made, the company must do, or be substantially compliant with, certain things. *[Schedule 1, item 1, regulation 5.3B.24(b)]*

In particular, the company must have paid all employee entitlements that are payable. The company must have also lodged all tax lodgements, notices, statements, applications or other documents as required by taxation laws (within the meaning of the *Income Tax Assessment Act 1997*) to the Australian Taxation Office. *[Schedule 1, item 1, regulation 5.3B.24(a)]*

This requirement to have paid all employee entitlements that are payable extends only to amounts which are payable, it does not require payment of amounts which may be owed but are not yet payable.

Employee entitlements are defined in sections 596AA(2) and (3) of the Corporations Act, and include wages, superannuation contributions, amounts due under an industrial instrument in respect of the employee's leave of absence and retrenchment payments, as well as amounts due in respect of injury compensation. *[Schedule 1, item 1, note to regulation 5.3B.24]*

This provision is an important safeguard that prevents a company with unpaid employee entitlements and that has not substantially complied with each tax lodgement from obtaining the benefit of the debt restructuring process. These requirements are consistent with the eligibility criteria for the simplified liquidation process.

A proposal to make a restructuring plan lapses

A company's proposal to make a restructuring plan lapses if creditors do not accept the plan, or the small business restructuring practitioner cancels the company's proposal to make a plan. *[Schedule 1, item 1, note to regulation 5.3B.20(1)]*

A small business restructuring practitioner for a company may cancel a company's proposal to make a plan if they become aware of any of the following before the plan is made:

- the information in the proposed restructuring plan is incomplete or inaccurate, and they believe on reasonable grounds that the incompleteness or inaccuracy is likely to affect the company's ability to meet their obligations under the plan;
- one or more affected creditors were not disclosed in the restructuring proposal statement for the proposed restructuring plan;
- the company's restructuring proposal statement for the proposed restructuring plan was deficient because a material particular of the statement was either omitted or incorrect; or
- a material change in the company's circumstances has occurred that:
 - was not foreshadowed in the company's restructuring proposal statement for the proposed restructuring plan; and
 - in the opinion of the small business restructuring practitioner, is capable of affecting an affected creditor's decision whether or not to accept the proposed restructuring plan.

[Schedule 1, item 1, regulation 5.3B.20(2)]

A material change in the circumstances of the company may include, for example, a change that is more than trivial, such as a change that could reasonably be expected to affect the affected creditor's decision whether or not to accept the proposed restructuring plan.

If the small business restructuring practitioner cancels the proposed plan before it is made, the plan lapses and the company's restructuring process is terminated.

[Schedule 1, item 1, regulation 5.3B.02(1)(c)]

Where a proposed restructuring plan lapses, the person who was the small business restructuring practitioner for the company immediately before the plan lapsed must, within two business days:

- lodge with ASIC, a notice in the prescribed form (if any) of the lapsing of the proposed plan, that the proposed restructuring plan has lapsed and the reasons why; and
- give a copy of the notice to as many creditors as reasonably practicable.

[Schedule 1, item 1, regulation 5.3B.53]

Accepting a proposal for a restructuring plan

For the proposed restructuring plan to be made, the small business restructuring practitioner must provide the restructuring plan, along with accompanying documents to creditors. If this does not occur within the proposal period, the company's restructuring process is terminated. *[Schedule 1, item 1, regulation 5.3B.02(1)(b)]*

The affected creditors have the opportunity to vote for the proposed restructuring plan. If a majority, by value, of the affected creditors whose replies are received by the small business restructuring practitioner before the end of the last day of the acceptance period accept the proposed restructuring plan, the plan is made. *[Schedule 1, item 1, regulation 5.3B.25]*

The ***acceptance period*** is either:

- 15 business days beginning on the day the small business restructuring practitioner gives the proposed restructuring plan and other prescribed documents to creditors;
- if the restructuring practitioner has provided a notice to creditors recommending that the schedule of debts and claims be varied because of a disagreement by a creditor concerning the amount of the creditor's admissible debts or claim—the longer of:
 - 15 business days beginning on the day the small business restructuring practitioner gives the required documents to creditors; and
 - the period beginning on the day the company's restructuring practitioner gives the required documents to creditors and ending on

the last day of the period of five business days after the day on which the notice is given; or

- such other period as is ordered by the Court.

[Schedule 1, item 1, regulation 5.3B.21(3)]

If the restructuring plan is rejected by a majority of the affected creditors whose replies are received by the restructuring practitioner before the end of the acceptance period, or cancelled by the practitioner for another reason, the plan lapses and the restructuring process is terminated. *[Schedule 1, item 1, regulation 5.3B.20(1)]*

The term **related creditor** means a creditor of the company who is also a ‘related entity’ of the company as defined in section 9 of the Corporations Act. *[Schedule 1, item 1, regulation 5.3B.01]*

Section 9 of the Corporations Act provides that a related creditor includes company directors and members and their relatives.

Giving the proposed plan to affected creditors

As soon as practicable following the execution of the restructuring plan by the company’s directors, the small business restructuring practitioner must give the proposed restructuring plan (and the other prescribed documents) to as many of the affected creditors as reasonably practicable. The prescribed documents are:

- the company’s proposed restructuring plan and restructuring proposal statement;
- the restructuring plan standard terms; and
- the certifying declaration prepared by the small business restructuring practitioner.

[Schedule 1, item 1, regulation 5.3B.21(1)(a)]

The small business restructuring practitioner must also ask each affected creditor to:

- give a written statement of whether or not they accept the proposed restructuring plan; and
- if the creditor agrees with the company’s assessment of the amount of the creditor’s admissible debts or claims—verify the creditor’s admissible debts or claims as set out in the restructuring plan; or
- if the creditor disagrees with the company’s assessment of the amount of the creditor’s admissible debts or claims—notify the restructuring practitioner in accordance with regulation 5.3B.20.

[Schedule 1, item 1, regulation 5.3B.21(1)(b)]

The small business restructuring practitioner must inform the affected creditors of the person to whom the statement should be given and of the need to do so before the end of the acceptance period. *[Schedule 1, item 1, regulation 5.3B.21(1)(c)]*

Since excluded creditors are unable to vote on the proposed restructuring plan, these creditors are not asked to provide a written statement to accept or reject the proposed restructuring plan. *[Schedule 1, item 1, regulation 5.3B.21(2)]*

Creditors' rights to dispute the schedule of debts and claims

The Regulations allow a creditor to dispute matters set out in the schedule of debts and claims included with the company's restructuring proposal statement. This applies where:

- the creditor is a creditor of a company that proposes to make a restructuring plan;
- the plan has not been made; and
- the creditor disagrees with the schedule of debts and claims included with the company's restructuring proposal statement because:
 - the creditor's admissible debts or claims are not specified;
 - the company's assessment of the creditor's admissible debts or claims is incorrect; or
 - the creditor has been incorrectly assessed as an excluded creditor.

[Schedule 1, item 1, regulation 5.3B.22(1)]

A creditor that seeks to dispute a matter may give a written notice of disagreement to the small business restructuring practitioner:

- if the creditor has received a copy of the restructuring plan, within five business days of receiving the plan;
- if the creditor has not received a copy of the restructuring plan but has otherwise become aware of it, within five business days of becoming aware; or
- after these periods provided the creditor also gives a statement explaining the reasons for not giving the notice within those specified periods. *[Schedule 1, item 1, regulation 5.3B.22(2) and (3)(a)]*

The Regulations prescribe what the creditor must include in the notice of the disagreement.

If the notice relates to the creditor's admissible debts or claims, it must include both:

- detailed particulars of the debt or claim sought to be proved; and

- if the disagreement relates to a debt—a statement of account and details of the vouchers (if any) by which the statement can be substantiated.

[Schedule 1, item 1, regulation 5.3B.22(3)(b)]

If the disagreement relates to the creditor’s status as an excluded creditor, the notice must include sufficient detail to resolve the disagreement. *[Schedule 1, item 1, regulation 5.3B.22(3)(c)]*

In order to properly assess the disagreement, the restructuring practitioner may, after receiving a notice of a disagreement, seek further information. Specifically, the restructuring practitioner may request that the creditor or the directors of the company give the restructuring practitioner information about the company’s business, property, affairs and financial circumstances. The restructuring practitioner may also request that the information is verified by statutory declaration. *[Schedule 1, item 1, regulation 5.3B.22(4)]*

The small business restructuring practitioner may refuse to consider the disagreement if the notice is provided after the specified period of five business days after a person becomes aware of the company’s restructuring plan, whether due to receipt of the restructuring plan or other means if the practitioner is satisfied that the creditor did not take all reasonable steps to give notice within the specified period. *[Schedule 1, item 1, regulation 5.3B.22(5)]*

If the small business restructuring practitioner refuses to consider the disagreement, the practitioner is taken to have recommended that the schedule of debts and claims in the restructuring proposal statement not be varied. The small business restructuring practitioner must provide a written notice to the creditor and the company setting out the reason for the refusal. *[Schedule 1, item 1, regulations 5.3B.22(6)(a) and (b)]*

Where the small business restructuring practitioner assesses the disagreement, the practitioner must give a written notice to the company and the creditor. The notice must set out the restructuring practitioner’s recommendations for resolving the disagreement and their reasons for the recommendations. *[Schedule 1, item 1, regulations 5.3B.22(7)(a) to (c)]*

If the restructuring practitioner recommends that the schedule of debts and claims be varied and is of the opinion that the variation is significant—the practitioner must state that fact in their recommendation notice. The notice must also outline the creditors’ rights to change their vote. *[Schedule 1, item 1, regulation 5.3B.22(7)(d)]*

If the small business restructuring practitioner refuses to consider the disagreement, the practitioner does not have to provide a notice of their recommendations. *[Schedule 1, item 1, regulation 5.3B.22(6)(c)]*

As soon as reasonably practicable after the restructuring practitioner recommends that the schedule of debts and claims be varied, the company must vary the schedule in accordance with the recommendation. *[Schedule 1, item 1, regulation 5.3B.22(8)]*

Creditors' rights to change their vote

The Regulations allow an affected creditor to change their vote on a proposed restructuring plan at any time before the end of the acceptance period. This applies where:

- a company proposes to make a restructuring plan; and
- an affected creditor gave a written statement setting out whether or not the restructuring plan should be accepted.

[Schedule 1, item 1, regulation 5.3B.23(1)]

The affected creditor may withdraw their statement and give a new statement in relation to the proposed restructuring plan. The affected creditor may change their statement at any time and as often as they want prior to the end of the acceptance period. *[Schedule 1, item 1, regulations 5.3B.23(2) to (4)]*

Court's power to settle a dispute regarding the proposed restructuring plan

Under section 458B of the Corporations Act, regulations may confer powers on the Court in relation to the restructuring of companies and restructuring plans. *[Schedule 1, item 1, regulation 5.3B.59]*

A creditor may apply to the Court if they disagree with the small business restructuring practitioner's refusal to consider the disagreement or recommendation in relation to a disagreement with the company's assessment of the value of a creditor's debt or claim. *[Schedule 1, item 1, regulation 5.3B.60(1)]*

The Court may, on application by the company or one of its creditors, make one or more of the following orders:

- that the restructuring practitioner to consider the disagreement and make a recommendation;
- that the schedule of debts and claims be varied (either adjusting the value of debt or claim, or the status of the creditor);
- that the acceptance period for the proposed restructuring plan be extended.

[Schedule 1, item 1, regulation 5.3B.60(2)]

Accepting the proposed restructuring plan by creditors

The proposed restructuring plan is **accepted** if, at the end of the last day of the acceptance period, a majority in value of the affected creditors from whom the small business restructuring practitioner has received a written statement under regulation 5.3B.21, state that the restructuring plan should be accepted. *[Schedule 1, item 1, regulations 5.3B.01 and 5.3B.25(1) and (5)]*

In assessing whether a majority in value has been met, the value of admissible debts or claims for a creditor is worked out with reference to:

- the value of the creditor’s admissible debts or claims known at the time the restructuring began; or
- if the creditor has purchased another creditor’s admissible debts or claims—the value of the purchase price.

[Schedule 1, item 1, regulation 5.3B.25(2)(a)]

In circumstances where there have been mutual credits, debts or other mutual dealings between the company and an affected creditor, the value of the admissible debt or claim is the balance of the accounts. This is worked out by taking an account of what is due from the one party to the other in respect of those mutual dealings and setting off the sum due from one party against any sum due from the other party.

[Schedule 1, item 1, regulation 5.3B.25(2)(b)]

The value of debts or claims of excluded creditors is disregarded in assessing if a majority of affected creditors have provided statements in relation to the proposed restructuring plan. *[Schedule 1, item 1, regulation 5.3B.25(2)(c)]*

The Regulations make it an offence for a person to give, or agree or offer to give, any valuable consideration to an affected creditor with the intention of affecting the acceptance or rejection of the proposed restructuring plan. This is a strict liability offence that carries a penalty of 50 penalty units. This offence has been made with regard to the Guide to Framing Commonwealth Offences. It is appropriate to ensure the integrity of the restructuring process and discourages misuse, by all parties, of the process. *[Schedule 1, item 1, regulations 5.3B.25(3) and (4)]*

Rejection by the affected creditors of the proposed restructuring plan

If a company’s proposal to make a restructuring plan is not accepted by the majority in value of the company’s affected creditors who voted, the proposal lapses and the company’s restructuring process ends. *[Schedule 1, item 1, regulations 5.3B.02(1)(c) and 5.3B.20(1)(a)]*

The effect of making a restructuring plan

A company’s restructuring process ends when the restructuring plan is made. *[Schedule 1, item 1, regulation 5.3B.02(1)(j)]*

When a restructuring plan is made

A restructuring plan is made when the proposed restructuring plan is accepted by the majority in value of affected creditors who voted during the acceptance period. *[Schedule 1, item 1, regulations 5.3B.26(1) and (4)]*

The parties to the restructuring plan are the company and the affected creditors. *[Schedule 1, item 1, regulation 5.3B.28]*

The restructuring plan is taken to be made on the day after:

- the end of a specified period within which a specified event must have occurred; or

- the acceptance period ends.

[Schedule 1, item 1, regulation 5.3B.26(2)]

Once a restructuring plan is made, it has the same force and validity as a deed executed by each party to the plan. *[Schedule 1, item 1, regulation 5.3B.26(3)]*

Failure to provide creditors with a notice of making the plan or to lodge the required information with ASIC is an offence under section 1311(1) of the Corporations Act.

Effect of a restructuring plan

On and after the day on which a restructuring plan is made, the restructuring plan binds creditors who have admissible debts or claims in relation to the plan, the company, the company's officers and members and the small business restructuring practitioner for the plan. *[Schedule 1, item 1, regulations 5.3B.29(1) and (2)]*

Secured creditors are only bound by the plan to the extent that they agree to be so bound, and that their admissible debts or claims exceeds the value of their security interest. *[Schedule 1, item 1, regulation 5.3B.29(3)]*

A secured creditor is not prevented from realising or otherwise dealing with their security interest after the restructuring plan is made, unless the secured creditor has accepted the proposal to make the plan and the plan prevents them from realising or dealing in the security interest or because a Court, under regulation 5.3B.64(2), orders a secured creditor of the company not to realise or otherwise deal with the security interest (see also section 454C(3) of the Corporations Act). *[Schedule 1, item 1, regulations 5.3B.29(4) and 5.3B.64]*

The right of an owner or lessor in relation to their property, except an owner or lessor of PPSA retention of title property of the company (see section 51F of the Corporations Act), is not affected by the making of a restructuring plan unless they accepted the plan and the plan affects that right, or the Court, under regulation 5.3B.64(4) ordered the owner or lessor of property that is used or occupied by, or is in the possession of, the company not to take possession of the property or otherwise recover it. *[Schedule 1, item 1, regulations 5.3B.29(5) and (6) and 5.3B.64(4)]*

Protections of the company and its property

While the restructuring plan is on foot, a person bound by the restructuring plan cannot make an application to wind up the company on the basis of an admissible debt or claim or proceed with such an application made before the plan became binding on the person. *[Schedule 1, item 1, regulations 5.3B.30(1) and (2)]*

In addition, a person bound by the plan cannot begin or proceed with a proceeding, or an enforcement process, against the company in relation to any of its property to recover an admissible debt or claim, unless they have Court leave to do so and act within any terms set by the Court. For this purpose, property of a company includes *Personal Property Securities Act 2009* retention of title property of the company (see section 51F of the Corporations Act) as well as any other property used or occupied by, or in the possession of the company (see section 9 of the Corporations Act). *[Schedule 1, item 1, regulations 5.3B.30(1), (3) and (4)]*

Rights, obligations and liabilities in relation to the restructuring practitioner

Section 456G of the Corporations Act provides that the regulations may make provision for the rights, obligations and liabilities of a company, its directors and officers in relation to the small business restructuring practitioner for the company. *[Schedule 1, item 1, regulation 5.3B.46]*

Terminating a debt restructuring plan

Under section 455B of the Corporations Act, the Corporations Regulations may prescribe circumstances in which a restructuring plan is terminated or contravened or when all or part of a restructuring plan is void, as well as the consequences of termination. *[Schedule 1, item 1, regulation 5.3B.13]*

Termination of a restructuring plan

The Regulations provide that a restructuring plan terminates:

- if all of the company's obligations under the plan and the obligations of any other party to the plan have been fulfilled, and all admissible debts or claims have been dealt with in accordance with the plan—on the day the obligations are fulfilled and the admissible debts or claims have been dealt with;
- if the Court makes an order to terminate the plan under regulation 5.3B.63 (further discussion below)—on the day specified in the order;
- if the plan is expressed to be subject to the occurrence of a specified event within a specified period of no longer than 10 business days after the plan is made, and that event does not occur within that period—on the next business day after the end of that period;
- if there has been a contravention of the plan by a person bound by the plan, and this has not been rectified within 30 business days beginning on the date of the contravention—on the next business day after the end of that period; or
- if an administrator, liquidator or provisional liquidator of the company is appointed—on the day of the appointment.

[Schedule 1, item 1, regulation 5.3B.31(1)]

Where the restructuring plan terminates because all obligations under the plan have been fulfilled, and all admissible debts or claims have been dealt with in accordance with the plan, the company is entitled to retain any property that was subject to the restructuring plan but was not required to be distributed to creditors. The company is also released from all admissible debts or claims that arose due to circumstances before the restructuring process began. *[Schedule 1, item 1, regulation 5.3B.31(2)]*

Effect of termination of a plan

The termination or avoidance of a restructuring plan, in whole or in part, does not affect the validity of anything done in good faith under the plan by a person prior to

the person having notice of the termination or avoidance. *[Schedule 1, item 1, regulation 5.3B.32]*

Powers of the Court to vary, void, validate and terminate a debt restructuring plan

Section 458A of the Corporations Act gives the Court a broad power to make orders as it thinks appropriate about how the new formal debt restructuring process in Part 3B of the Corporations Act should operate in relation to a particular company. Section 458B of the Corporations Act also provides that regulations may confer other powers on the Court, including specific powers for the Court to vary, void, validate or terminate a restructuring plan. *[Schedule 1, item 1, regulation 5.3B.59]*

The Court may vary a restructuring plan

Where a restructuring plan has already been made, it may only be varied by Court order under regulation 5.3B.61. The Court may make an order varying a restructuring plan on its own initiative or on the application of the company, an affected creditor, the restructuring practitioner for the plan, or ASIC. *[Schedule 1, item 1, regulation 5.3B.61]*

The Court may void a restructuring plan

The Court may also make an order declaring that all or part of a company's restructuring plan is void. The Court may make any other order that it thinks appropriate in relation to the declaration. The Court may make such an order if it is satisfied of one or more of the following:

- there are reasonable grounds to believe that the whole, or part, of the plan was not made in accordance with, or does not comply with, the Corporations Act or the Corporations Regulations;
- the small business restructuring practitioner for the plan has committed a breach of duty in relation to the restructuring plan;
- the small business restructuring practitioner for the plan has breached a condition of their registration as a liquidator; or
- the small business restructuring practitioner for the plan breaches a condition imposed on their registration as a registered liquidator (see section 20-35 of the Schedule 2 to the Corporations Act (the Insolvency Practice Schedule)) to the extent the condition relates to the restructuring plan.

[Schedule 1, item 1, regulations 5.3B.62(1) and (2)]

The Court may make an order voiding a restructuring plan on the application of the company, an affected creditor, the company's restructuring practitioner, or ASIC. However, an application must not be made if the plan has terminated because of regulation 5.3B.31(1)(a) (relating to circumstances where all obligations have been fulfilled and all admissible debts or claims have been dealt with). [Schedule 1, item 1, regulations 5.3B.62(4) and (5)]

The Court may validate a restructuring plan

The Court may make an order declaring the whole, or part, of the restructuring plan valid despite a contravention of a provision of the Corporations Act or the Corporations Regulations. The Court may make such an order if satisfied that the provision was substantially complied with and no injustice will result for anyone bound by the plan if the contravention is disregarded. [Schedule 1, item 1, regulation 5.3B.62(3)]

The Court may make an order validating a restructuring plan on the application of the company, an affected creditor, the company's restructuring practitioner, or ASIC. However, an application must not be made if the plan has terminated because of regulation 5.3B.31(1)(a) (relating to circumstances where all obligations have been fulfilled and all admissible debts or claims have been dealt with). [Schedule 1, item 1, regulations 5.3B.62(4) and (5)]

The Court may terminate a restructuring plan

The Court may make an order terminating the restructuring plan. The Court may make such an order if it is satisfied of one or more of the following:

- information about the company's business, property, affairs or financial circumstances that was contained in the proposed restructuring plan or restructuring proposal statement was false or misleading and the information can reasonably be expected to have affected the decision of affected creditors to accept the proposed restructuring plan;
- there was an omission from the proposed restructuring plan or restructuring proposal statement that could reasonably be expected to have been material in the decision to accept the proposed restructuring plan;
- there has been a material contravention by a person bound by the restructuring plan;
- the plan cannot be given effect without injustice or undue delay;
- the plan or a provision of it is, an act or omission done or made under the plan was, or an act or omission proposed to be so done or made, would be contrary to the interests of creditors of the company as a whole; or
- the plan should be terminated for some other reason.

[Schedule 1, item 1, regulation 5.3B.63(1)]

The Court may make an order terminating a restructuring plan on the application of the company, an affected creditor, the company's restructuring practitioner or the restructuring practitioner for the plan, or ASIC. The Court may also make an order terminating the restructuring plan on its own initiative. [Schedule 1, item 1, regulation 5.3B.63(2)]

Small business restructuring practitioner for a restructuring plan

Section 455B(7) of the Corporations Act provides that the Corporations Regulations may provide for matters relevant to appointing a small business restructuring practitioner for a restructuring plan. This includes their functions, duties and powers in relation to the restructuring plan, and the rights, obligations and liabilities of the small business restructuring practitioner arising out of the performance of their functions and duties and the exercise of their powers.

Appointing a small business restructuring practitioner for a restructuring plan

When a restructuring plan is made, the appointment of a person as the small business restructuring practitioner for the company terminates, and the person is automatically appointed as the small business restructuring practitioner for the plan, unless the company's board resolves otherwise. [Schedule 1, item 1, regulation 5.3B.33]

Under sections 456A and 456B of the Corporations Act, a person cannot be appointed as a small business restructuring practitioner for a restructuring plan unless the person has consented in writing to the appointment and, as of the time of their appointment, the person has not withdrawn their consent. Only a registered liquidator can consent to be a small business restructuring practitioner.

Vacancy in the office

A restructuring practitioner for a company's restructuring plan may be replaced in prescribed circumstances. Someone else may be appointed where the restructuring practitioner dies, becomes prohibited from acting as restructuring practitioner for the plan, or resigns by notice in writing given to the company. In these circumstances, a replacement appointment may be made by the appointer. [Schedule 1, item 1, regulation 5.3B.34(1)]

The **appointer** in these circumstances is

- the Court; or
- the company by resolution of the board.

[Schedule 1, item 1, regulations 5.3B.34(2) and (3)]

The appointer may be the Court where:

- the restructuring practitioner was appointed by the Court under Division 90 of the Insolvency Practice Schedule (relating to the review of the external administration of a company); or

- the company has made a restructuring plan, but for some reason no restructuring practitioner for the plan is acting and ASIC or an officer, member or creditor of the company makes an application to the Court to make an appointment.

[Schedule 1, item 1, regulations 5.3B.34(2) and (4)]

Declarations by new and replacement restructuring practitioners

Under sections 453D and 453F of the Corporations Act, a small business restructuring practitioner must make a declaration of relevant relationships when appointed and provide it to the company's creditors and ASIC. This information must be accurate, complete and kept up-to-date throughout the debt restructuring process. Any amendments to the declaration must be provided to creditors and ASIC as soon as practicable. This is also the case for a replacement small business restructuring practitioner for a company.

The Regulations extend this requirement to the appointment of a replacement small business restructuring practitioner to a plan.

A new or replacement restructuring practitioner for the plan is to make a declaration of relevant relationships as soon as practicable after being appointed. The new or replacement practitioner must lodge a copy of the declaration with ASIC as soon as practicable after their appointment and give the declaration to as many of the company's creditors as reasonably practicable. Failure to make the declaration or provide copies to ASIC and creditors is an offence under section 1311(1) of the Corporations Act. [Schedule 1, item 1, regulations 5.3B.35(1) to (4)]

A defence is available for the failure to include a particular matter in a declaration where the new or replacement restructuring practitioner for the plan makes reasonable enquiries and, on the basis of those enquiries, has no reasonable grounds to believe that the matter should be included in the declaration. [Schedule 1, item 1, regulation 5.3B.35(5)]

If a small business restructuring practitioner's declaration of relevant relationships becomes out-of-date or the practitioner identifies an error, the practitioner must, as soon as practicable, make a replacement declaration and lodge a copy with ASIC and give a copy to as many of the company's creditors as reasonably practicable. Failure to update and ensure accuracy of the declaration of relevant relationships and lodge a copy with ASIC and provide a copy to creditors is an offence under section 1311(1) of the Corporations Act. [Schedule 1, item 1, regulations 5.3B.36(1) to (3)]

A defence for a failure to make a replacement declaration is available where the new or replacement restructuring practitioner for the plan makes reasonable enquiries and, on the basis of those enquiries, has no reasonable grounds to believe that the matter should be included in the declaration. [Schedule 1, item 1, regulation 5.3B.36(4)]

Functions of the restructuring practitioner for a restructuring plan

While the restructuring practitioner appointed for the company during the restructuring process has a largely supportive role in advising and assisting the company directors, the restructuring practitioner appointed for the plan has functions necessary for administering the plan.

The Regulations prescribe the following functions of a restructuring practitioner for a restructuring plan:

- receiving money from, and holding money on trust for, the company;
- paying money to creditors in accordance with the plan;

- if requested by the company’s directors:
 - realising any property available to pay creditors in accordance with the plan; and
 - distributing the proceeds of such realisation among creditors in accordance with the plan;
- answering questions about the performance or exercise of their functions and powers as the small business restructuring practitioner for the plan, and doing anything incidental to the performance of those functions and powers; and
- doing anything else that is necessary or convenient for the purpose of administering the plan.

[Schedule 1, item 1, regulation 5.3B.37]

Lodgement of outstanding notices

Where a vacancy arises in the office of small business restructuring practitioner for the restructuring plan, a replacement small business restructuring practitioner – known as the **replacement practitioner** – can be appointed. The replacement practitioner must do things that were required to be done, but were not done, by the previous small business restructuring practitioner. The replacement practitioner must do the things within two business days after being appointed or within two business days after being given the notice or becoming aware of the thing that is required to be done. *[Schedule 1, item 1, regulation 5.3B.38(1) and (2)]*

For the purposes of this requirement, the things that must be done are things that were required to be done by the previous small business restructuring practitioner but were not done under:

- Division 4 of the Corporations Regulations (relating to notification that the company is not likely to discharge its obligations under the plan or the appointment of an administrator, liquidator or provisional liquidator); or
- Subdivision B or C of Division 5 of the Corporations Regulations (relating to information, reports and documents during restructuring and information, reports and documents once the restructuring plan is made).

[Schedule 1, item 1, regulation 5.3B.38(2)]

Disposal of company property

As mentioned above, in the course of undertaking their functions, the small business restructuring practitioner for a plan may dispose of company property in order to make payments to creditors in accordance with the plan. *[Schedule 1, item 1, regulation 5.3B.37]*

However, a practitioner must not dispose of property that is subject to a security interest. The practitioner must also not dispose of property that is used or occupied by, or in possession of, the company but where someone else is the owner or lessor. *[Schedule 1, item 1, regulation 5.3B.39(1)]*

In cases where someone else is the owner or lessor of the property, the prohibition on the disposal of the property under regulation 5.3B.39 does not apply to PPSA retention of title property (see section 51F of the Corporations Act). PPSA retention of title property is subject to a PPSA security interest, and so is covered by the prohibition on the disposal of property that is subject to a security interest in regulation 5.3B.39(1)(a). *[Schedule 1, item 1, regulations 5.3B.39(1) and (2)]*

The prohibition on the disposal of property that is subject to a security interest or that is owned or leased by someone else does not apply if the disposal occurs:

- in the ordinary course of business for the company;
- with the written consent of the secured party, owner or lessor; or
- with the leave of the Court.

[Schedule 1, item 1, regulation 5.3B.39(2)]

For the Court to give leave, the Court must be satisfied that arrangements have been made to adequately protect the interests of the secured party, owner or lessor.

[Schedule 1, item 1, regulation 5.3B.39(3)]

Where a restructuring practitioner proposes to dispose of property because it is in the ordinary course of the company's business, the Court may order the practitioner not to carry out the proposal if it is not satisfied that arrangements have been made to adequately protect the interests of the applicant for the order. The Court may make such an order on the application of the secured party or the owner or lessor of the property, as the case may be. *[Schedule 1, item 1, regulations 5.3B.39(4) to (6)]*

Also in relation to the disposal of property in the ordinary course of the company's business, if the owner of the property demands the return of the property, a disposal of the property that occurs after the demand is made does not mean that the disposal is not in the ordinary course of the company's business. This applies where property is used or occupied by, or is in the possession of, a company, another person is the owner of the property, and the property is either PPSA retention of title property or subject to a retention of title clause under a contract. *[Schedule 1, item 1, regulation 5.3B.39(8)]*

Where a restructuring practitioner disposes of property that is subject to a security interest, the disposal extinguishes the security interest. This applies where the company has made a restructuring plan that has not terminated. *[Schedule 1, item 1, regulation 5.3B.39(7)]*

Restructuring practitioner acts as a company's agent

When performing a function or duty, or exercising a power, as restructuring practitioner for a company's restructuring plan, the restructuring practitioner is taken to be acting as the company's agent. *[Schedule 1, item 1, regulation 5.3B.40]*

Qualified privilege and protection from liability for a small business restructuring practitioner for a company subject to a plan

The Regulations prescribe that a person who is or has been a small business restructuring practitioner for a plan has qualified privilege in respect of a statement made, orally or in writing, in the course of performing or exercising any of their functions and powers as a small business restructuring practitioner for the plan. *[Schedule 1, item 1, regulation 5.3B.41]*

The provision of qualified privilege to a restructuring practitioner is consistent with the privilege afforded to liquidators during winding up and administrators during voluntary administration.

The Regulations also prescribe that a person who is or has been a small business restructuring practitioner for a plan is not subject to any liability to any person in respect of anything done, or omitted to be done, in good faith and without negligence in the exercise or performance, or the purported exercise or performance, of powers, functions or duties under the Corporations Act or the Corporations Regulations relating to the plan. *[Schedule 1, item 1, regulation 5.3B.42]*

This protection from liability includes protection where a small business restructuring practitioner must undertake functions, powers or duties following the termination of their appointment. This arises where a person must fulfil notice requirements following the termination of a restructuring plan, or where a restructuring process ends prior to making a plan.

Protection from liability is an important safeguard intended to ensure that practitioners are able to undertake their functions, including investigating and reporting on the affairs of the company, without risk of legal proceedings.

Right of indemnity – general rule

A person who is or has been the restructuring practitioner for a company's restructuring plan is entitled to be indemnified out of the company's property, except for property that is PPSA retention of title property subject to a PPSA security interest that is perfected within the meaning of the *Personal Property Securities Act 2009*. *[Schedule 1, item 1, regulation 5.3B.43]*

The right of indemnity applies to any debts or liabilities incurred or damages or losses sustained in the performance or purported performance of a practitioner's functions or duties or in the exercise or purported exercise of their power. They are also indemnified in relation to remuneration they are entitled to under Subdivision DA of Division 60 of the Insolvency Practice Schedule (relating to remuneration of restructuring practitioners). The right of indemnity does not cover acts that are not performed in good faith or that are negligent. *[Schedule 1, item 1, regulation 5.3B.43]*

The small business restructuring practitioner's right of indemnity has priority over:

- all of the company's unsecured debts;

- any debts of the company secured by a PPSA security interest in property of the company if, when the restructuring of the company begins, the security interest is vested in the company because of the operation of section 267 or 267A of the *Personal Property Securities Act 2009* (property subject to unperfected security interests) or section 588FL of the Corporations Act (collateral not registered within time); and
- unless regulation 5.3B.44 provides otherwise—debts of the company secured by a circulating security interest in property of the company.

[Schedule 1, item 1, regulation 5.3B.44(1)]

This general rule of priority is subject to section 556 of the Corporations Act (dealing with priority payments). *[Schedule 1, item 1, regulation 5.3B.44(1)]*

Right of indemnity – debts secured by circulating security interests

The priority that the right of indemnity has over other debts differs where the debt is secured by a circulating security interest, and where other circumstances exist.

Receiver appointed before the beginning of restructuring

Where a debt is secured by a circulating security interest, a right of indemnity under regulation 5.3B.43 has priority over the secured debt only so far as the secured party agrees. This applies if:

- before making the restructuring plan, the secured party:
 - appointed a receiver of property of the company under a power contained in an instrument relating to the security interest;
 - obtained an order for the appointment of a receiver of property of the company for the purpose of enforcing the security interest;
 - entered into possession, or assumed control, of property of the company for that purpose; or
 - appointed a person so as to enter into possession or assume control of property of the company (whether as agent for the secured party or for the company); and
- the receiver or person is still in office, or the secured party is still in possession or control of the property.

[Schedule 1, item 1, regulation 5.3B.44(2)]

Receiver appointed after the restructuring plan is made

A right of indemnity of the restructuring practitioner under regulation 5.3B.43 has priority over debts of the company that are secured by a circulating security interest in property of the company only in so far as it is a right of indemnity for debts incurred, or remuneration accruing, before written notice of the appointment, or of

the entering into possession or assuming of control, as the case may be, was given to the restructuring practitioner. *[Schedule 1, item 1, regulation 5.3B.44(4)]*

This rule applies if:

- debts of the company are secured by a circulating security interest in property of the company; and
- after the company's restructuring plan is made, the secured party, consistently with Part 5.3B of the Corporations Act (dealing with the restructuring of a company):
 - appoints a receiver of property of the company under a power contained in an instrument relating to the security interest;
 - obtains an order for the appointment of a receiver of property of the company for the purpose of enforcing the security interest;
 - enters into possession, or assumes control, of property of the company for that purpose; or
 - appoints a person to enter into possession or assume control of property of the company (whether as agent for the secured party or for the company).

[Schedule 1, item 1, regulation 5.3B.44(3)]

Priority over right of indemnity in relation to repayment of money borrowed

Except so far as the secured party consents in writing, a right of indemnity under regulation 5.3B.43 does not have priority over debts of the company that are secured by a circulating security interest in property of the company to the extent that the right of indemnity relates to debts incurred for:

- the repayment of money borrowed;
- interest in respect of money borrowed; or
- borrowing costs.

[Schedule 1, item 1, regulation 5.3B.44(5)]

Lien to secure indemnity

To secure the right of indemnity under regulation 5.3B.43, the restructuring practitioner has a lien on the company's property. The lien has priority over another security interest only in so far as the right of indemnity under regulation 5.3B.43 has priority over debts secured by the other security interest. *[Schedule 1, item 1, regulation 5.3B.45]*

Notice requirements

Section 457A of the Corporations Act enables the Corporations Regulations to prescribe a number of notice requirements in relation to the restructuring plan. These notice requirements keep creditors and ASIC informed when a proposed restructuring plan has lapsed, and when a restructuring plan is made, varied or terminated. *[Schedule 1, item 1, regulation 5.3B.48]*

Notice of restructuring plan

The small business restructuring practitioner must lodge with ASIC in the prescribed form (if any), the restructuring plan, restructuring proposal statement and the certifying declaration, within two business days after giving them to creditors (see regulation 5.3B.21). *[Schedule 1, item 1, regulation 5.3B.52]*

Notice of appointment of a restructuring practitioner for a plan

Within two business days after being appointed, the restructuring practitioner for the plan must lodge notice of the appointment with ASIC in the prescribed form (if any) and in accordance with regulation 5.6.75(4) (dealing with publication in the prescribed manner). *[Schedule 1, item 1, regulation 5.3B.54]*

Notice of making a restructuring plan

Where a restructuring plan has been made by the company, the small business restructuring practitioner for the plan must, within two business days:

- notify each creditor in writing that a restructuring plan has been made and the date that the plan was made; and
- lodge with ASIC, the following:
 - a notice in the prescribed form (if any) of the making of the plan;
 - information about the total value of the debts and claims of the company;
 - details of the number of creditors to whom the proposal to make a restructuring plan was sent; and
 - the proportion in value of the company's affected creditors who stated before the end of the acceptance period that the plan should be accepted.

[Schedule 1, item 1, regulation 5.3B.55]

Notice of Court orders in relation to creditor disputes

Where there has been a variation to the restructuring plan by a Court order in relation to a creditor dispute, the small business restructuring practitioner for the plan must, within two business days:

- notify as many creditors as reasonably practicable, in writing, setting out the terms of the Court order and outlining the creditors' rights; and
- lodge with ASIC, a notice in the prescribed form (if any) about the variations to the restructuring plan.

[Schedule 1, item 1, regulation 5.3B.60(3)]

Notice of certain matters

The directors of a company that has made a restructuring plan that has not terminated must notify the small business restructuring practitioner for the plan within two business days if they become aware that:

- the company is not likely to be able to meet its obligations under the plan as and when they are due and payable; or
- an administrator, liquidator or provisional liquidator of the company is appointed.

[Schedule 1, item 1, regulations 5.3B.47(1) and (3)]

Within two business days after receiving notice (that the company is not likely to be able to meet its obligations under the plan or that an administrator, liquidator or provisional liquidator of the company is appointed), the restructuring practitioner for the plan must to lodge a notice with ASIC in the prescribed form (if any) and give a copy of this notice to as many of the company's creditors as reasonably practicable.

[Schedule 1, item 1, regulation 5.3B.47(2)]

Notice of contravention of a restructuring plan

Where a director of the company becomes aware of a contravention or a likely contravention of the plan by a person bound by the plan (who may be the director), the director must, within two business days after becoming aware, give written notice to the restructuring practitioner for the plan. *[Schedule 1, item 1, regulation 5.3B.56(1)]*

The small business restructuring practitioner must lodge with ASIC a notice of the contravention or likely contravention. The notice must be in the prescribed form (if any) and must be lodged within two business days after the day on which the restructuring practitioner receives the notice from the director or otherwise becomes aware of the contravention or likely contravention. The practitioner must also give a copy of the notice to as many of the company's creditors as reasonably practicable.

[Schedule 1, item 1, regulation 5.3B.56(2)]

Notice of termination of a restructuring plan

If a restructuring plan terminates because the obligations of the company and other parties under the plan have been fulfilled and because all admissible debts and claims have been dealt with (see regulation 5.3B.31(1)(a)), notice must be given of the termination. *[Schedule 1, item 1, regulation 5.3B.57(1)]*

In these circumstances, the directors of the company must give written notice of the termination to the person who was the restructuring practitioner for the plan immediately before the termination (the former practitioner). The notice must be given within two business days after the day on which the directors become aware of the happening of the event that causes the restructuring to terminate. *[Schedule 1, item 1, regulation 5.3B.57(1)(a)]*

The former practitioner must notify ASIC of the termination by lodging with ASIC notice in the prescribed form (if any). The former practitioner must also give a copy of the notice to as many of the company's creditors as reasonably practicable. The notice to ASIC and to creditors must be given within two business days after the day on which the former practitioner receives the notice from the directors. *[Schedule 1, item 1, regulation 5.3B.57(1)(b)]*

Notice of the termination must also be given if the termination occurs under regulation 5.3B.31(1) other than under regulation 5.3B.31(1)(a). *[Schedule 1, item 1, regulation 5.3B.57(2)]*

In these circumstances, the directors of the company must give written notice of the termination to the former practitioner. The notice must be given within two business days after the day on which the directors become aware of the happening of the event that causes the restructuring to terminate. *[Schedule 1, item 1, regulation 5.3B.57(2)(a)]*

The former practitioner must notify ASIC of the termination by lodging with ASIC notice in the prescribed form (if any). The notice must include the reason for the termination. The former practitioner must also give a copy of the notice to as many of the company's creditors as reasonably practicable. The notice to ASIC and to creditors must be given within two business days after the day on which the former practitioner receives the notice from the directors. *[Schedule 1, item 1, regulation 5.3B.57(2)(b)]*

Notice of termination of appointment of a restructuring practitioner for a plan

Where the appointment of a small business restructuring practitioner for the plan ends, the practitioner must give notice to ASIC in the prescribed form (if any). The notice must be given within two business days after the day on which the appointment ends. If the appointment ends because the practitioner dies, notice must be given to ASIC by the company. *[Schedule 1, item 1, regulation 5.3B.58]*

Failure to comply

Failure to comply with each of the notice requirements outlined above is an offence under section 1311(1) of the Corporations Act.

Consequential amendments

The publication website

The Corporations Regulations provides a framework enabling ASIC to maintain a *publication website*, as defined in regulation 5.6.75 in the Corporations Regulation, on which it publishes notices that are required to be published in the prescribed manner under various Parts of the Corporations Act, including Parts in Chapter 5— External administration.

The Regulations amend regulation 5.6.75 to allow notices that are required to be published under new Part 5.3B to be published on ASIC’s publication website in the manner prescribed by regulation 5.6.75. *[Schedule 1, item 2, regulation 5.6.75(1)(a)]*

Schedule 2 – Amendments relating to temporary restructuring relief

Division 7 of Part 5.3B of the Corporations Act establishes a period of temporary relief for an eligible company seeking to enter the new debt restructuring process. Schedule 2 to the Regulations makes amendments to the Corporations Regulations to prescribe matters relevant to the operation of the temporary restructuring relief.

All legislative references in this Schedule are to the Corporations Regulations unless otherwise specified.

Temporary increase to the statutory minimum and statutory period

For a company that is eligible for temporary restructuring relief, the Regulations prescribe a statutory minimum and a statutory period for the purposes of section 9 of the Corporations Act.

The statutory minimum prescribed is \$20,000 and the statutory period prescribed is six months. *[Schedule 2, item 1, regulation 5.4.01AAA]*

The higher amount and the longer period reflect the intention that a company seeking to enter the restructuring process receives appropriate relief against a creditor's statutory demand for the payment of a debt.

The regulation prescribing the higher statutory minimum and the longer statutory period is repealed at the end of the period of seven months starting on the day regulation 5.4.01AAA commences – no company is able to be eligible for temporary restructuring relief beyond this date (see section 458E of the Corporations Act). *[Schedule 2, item 1, regulation 5.4.01AAA]*

The Regulations also amend two of the notes in Form 509H (Creditor's statutory demand for payment of debt) in Schedule 2 to the Corporations Regulations to provide that, for a period in 2021 and where the debtor company is eligible for temporary restructuring relief, the statutory minimum is \$20,000 and the statutory period is six months. *[Schedule 2, items 2 and 3, notes 2 and 5 in Form 509H in Schedule 2]*

Schedule 3 – Amendments relating to the simplified liquidation process

Subdivision B of Division 3 of Part 5.5 of the Corporations Act establishes the new simplified liquidation process. Schedule 3 to the Regulations makes amendments to the Corporations Regulations to prescribe matters relevant to the operation of the simplified liquidation process.

All legislative references in this Schedule are to the Corporations Regulations unless otherwise specified.

Declaration that the company is eligible and other matters for the simplified liquidation process

Section 498 of the Corporations Act provides that the directors of a company must give the liquidator a declaration stating that the directors believe on reasonable grounds that the eligibility criteria for the simplified liquidation process will be met in relation to the company. The Corporations Act also provides that the declaration must include any information prescribed in the Corporations Regulations (see sections 498(2)(c) and 498(3) of the Corporations Act). The Regulations prescribe the following information as information that must be included in the director's declaration:

- whether, in the directors' opinion, there are reasonable grounds to believe that the company has, at any time, entered into a transaction that is a voidable transaction of a kind that is an uncommercial transaction, an unfair loan to a company, an unreasonable director-related transaction or a creditor-defeating disposition (see sections 588FB, 588FD, 588FDA and 588FDB of the Corporations Act); and
- whether, in the directors' opinion, there are reasonable grounds to believe that, on the declaration being given, the eligibility criteria for the simplified liquidation process will be met in relation to the company, and the reasons for that opinion.

[Schedule 3, item 2, regulation 5.5.02]

The requirement, described above, that directors declare that they have not entered into the transactions and believe on reasonable grounds that the eligibility criteria will be met is intended to provide the liquidator with information to inform their assessment of whether the eligibility criteria for the simplified liquidation process are met and whether the company has engaged in conduct of the sort that would make the adoption of the simplified liquidation process unsuitable or inappropriate.

If a director provides false or misleading information in the declaration, the director may be subject to civil or criminal penalties under section 1308 of the Corporations Act. These are existing penalties within the Corporations Act penalties framework, and provide an appropriate level of deterrence in relation to directors providing information to the liquidator that may be false or misleading.

Eligibility criteria for the simplified liquidation process

The Regulations prescribe a number of matters relevant to the eligibility for the simplified liquidation process.

Liabilities test of the company

Section 500AA of the Corporations Act empowers the Corporations Regulations to prescribe a test for eligibility for the simplified liquidation process based on the liabilities of the company.

The Regulations prescribe that the test based on liabilities is that the total liabilities of the company on the day on which the triggering event occurred must not exceed \$1 million (for triggering events – see section 489F of the Corporations Act). The meaning of liabilities includes any liability or obligation. *[Schedule 3, item 2, regulations 5.5.03(1) and (6)]*

Circumstances in which the previous use rule does not apply

The eligibility criteria for the simplified liquidation process in section 500AA of the Corporations Act requires that, subject to exceptions prescribed in the Corporations Regulations, the simplified liquidation process cannot be used in either of the following scenarios:

- where a director of the company has been a director of a company that has undergone restructuring or been the subject of a simplified liquidation process;
- where the company itself has undergone restructuring or been the subject of a simplified liquidation process.

In part, these rules are designed to target illegal phoenixing and other high risk behaviours.

Phoenix activity can encompass both legitimate business rescue activities and the use of serial deliberate insolvency as a business model to avoid paying company debts. While the scale of illegal phoenix activity ranges from the opportunistic to the systemic, a common characteristic is the stripping and transfer of assets from a company to another entity. Such transactions are carried out by a company's directors or other controlling minds with the intention of defeating the interests of the first company's creditors in that company's assets. Such transactions are also facilitated by others, including unscrupulous pre-insolvency advisers or other business advisers, who advise companies on how to engage in illegal phoenix activity. In many cases a new company is then started to continue with the same or similar business activities without the existing debt.

Some examples of signs that can point to illegal phoenix activity include:

- employees have transferred to a new company;
- company directors have been involved with liquidated entities before;

- requests for payments or contracts to be paid to a new company;
- recent changes to a company's directors including the use of straw or dummy directors;
- assets disposed of prior to liquidation not at market value to related entities or parties.

The rule against previous use of restructuring or simplified liquidation is particularly designed to target the potential indicator of illegal phoenix behaviour where company directors have been involved with liquidated entities before. However, in some circumstances, previous involvement with liquidated entities is not considered a potential indicator of illegal phoenix behaviour. To address these circumstances, the Regulations prescribe circumstances in which the previous use rule in section 500AA of the Corporations Act does not apply.

Previous use more than seven years ago

Section 500AA empowers the Corporations Regulations to prescribe the period in which the previous use must not have occurred (hereafter referred to as the 'previous use rule').

The Regulations prescribe a period of seven years as the period in which the previous use rule applies. This means that a director or company is not prohibited from being eligible for the simplified liquidation process where the director or company previously used the restructuring process or the simplified liquidation process more than seven years prior to the current company seeking to satisfy the eligibility criteria for the simplified liquidation process. *[Schedule 3, item 2, regulations 5.5.03(2) and (3)]*

Previous use by a related body corporate

Section 500AA also empowers the Corporations Regulations to prescribe circumstances in which a director or a company is exempt from the previous use rule.

In relation to previous use by a director, the Regulations prescribe the following circumstances:

- the other company of which the person was or is a director is a related body corporate of the current company seeking to satisfy the eligibility criteria for the simplified liquidation process;
- if the other company is or has been undergoing restructuring—the restructuring practitioner was appointed no more than 20 business days before the day on which the current company adopted the simplified liquidation process. The restructuring of a company begins when a restructuring practitioner for the company is appointed under section 453B of the Corporations Act;
- if the other company is or has been the subject of the simplified liquidation process—there is no more than 20 business days between the day on which both companies adopted the simplified liquidation process.

[Schedule 3, item 2, regulation 5.5.03(4)]

In this circumstance, the intention is to allow companies that are related to each other, (for example, in the same corporate group) to restructure or use the simplified liquidation process at the same or roughly the same time. This reflects the likelihood that if a company within a corporate group is insolvent or likely to become insolvent, other companies within the group may need to restructure or liquidate at the same or roughly the same time. In many instances, these related companies will have common directors. The term ‘related body corporate’ includes a company that is a holding company or subsidiary of the other (see sections 9 and 50 of the Corporations Act).

In relation to previous use by a company, the Regulations prescribe the following circumstances:

- the company has been undergoing restructuring; and
- the restructuring terminated no more than 20 business days before the day on which the current company adopted the simplified liquidation process (for when restructuring ends, see regulation 5.3B.02).

[Schedule 3, item 2, regulation 5.5.03(5)]

In this circumstance, the intention is to allow a company that has recently terminated a restructuring to enter into the simplified liquidation process, provided that the movement into liquidation happens soon after the termination of the restructuring process.

The 25 per cent in value of creditors test

A liquidator must not adopt the simplified liquidation process if at least 25 per cent in value of creditors request the liquidator not to follow the simplified liquidation process in relation to the company (see sections 500A(2)(c) and 500AD of the Corporations Act). Section 500AD(b) of the Corporations Act empowers the Corporations Regulations to prescribe creditors that are, or are not, to be taken into account for the purposes of the test.

The Regulations prescribe a person who is a related entity, and a creditor, of the company is not to be taken into account for the purposes of the 25 per cent in value test. The term ‘related entity’ in relation to a body corporate is defined in section 9 of the Corporations Act. The term captures a wide group of people and entities, including people involved with the formation and management of the company, and people in a family relationship with such people. The exclusion of a creditor who is a related entity of the company reflects the intention that the necessary 25 per cent in value should be properly representative of the views of creditors generally, and not inappropriately influenced by creditors who may have a less than arms-length relationship with the company. *[Schedule 3, item 2, regulation 5.5.09]*

Voidable transactions

Where a company which is unable to pay its debts as they fall due enters into a transaction with a creditor which has the effect of providing that creditor with an advantage in repayment over that which it would receive if the transaction were set

aside and the creditor were to prove for the debt in the winding-up, and where the transaction was entered into within six months before the relation-back day—then the transaction is an unfair preference and may be voidable. For a creditors' voluntary winding up, the relation-back day is generally the day on which the resolution to wind up the company was passed (see sections 9, 91 and 513B of the Corporations Act). The rationale underpinning unfair preferences is to enforce equal treatment among creditors by invalidating transactions between an insolvent debtor corporation and a creditor that have been made prior to liquidation, and that have the effect of preferring that creditor over creditors in general. See section 588FA of the Corporations Act.

Where a company is being wound up, a transaction of the company that was entered into on or after the relation-back day may be voidable. If it appears to a liquidator that a company which is being wound up has entered into a voidable transaction, the liquidator may seek an order of the Court to have the transaction set aside. If the Court is satisfied that the transaction is voidable it has the power to make any of the orders under section 588FF of the Corporations Act. These orders are designed to restore the company to the position it would have been in if it had not entered into the voidable transaction. See section 588FE of the Corporations Act.

In relation to a liquidation that has adopted the simplified liquidation process, section 500AE(3)(b) of the Corporations Act enables the Corporations Regulations to prescribe circumstances in which a transaction is not voidable despite section 588FE of the Corporations Act.

The Regulations insert regulation 5.5.04 to provide that, in a simplified liquidation process, a transaction is not voidable under section 588FE(2) of the Corporations Act in the following two circumstances. *[Schedule 3, item 2, regulation 5.5.04]*

First, a transaction is not voidable in a simplified liquidation process where:

- the transaction is an unfair preference;
- the transaction was entered into more than three months prior to the relation-back day; and
- no creditor under the transaction is a related entity of the company.

[Schedule 3, item 2, regulations 5.5.04(2) and (3)]

The effect of this is that, for transactions that occurred more than three months before the relation-back day, an unfair preference is only voidable in a simplified liquidation process if a creditor under the transaction was a related entity of the company.

Second, a transaction is not voidable in a simplified liquidation process where:

- the transaction is an unfair preference;
- the transaction was entered into during the three months prior to the relation-back day, or after that day but before the winding up began;

- no creditor under the transaction is a related entity of the company; and
- the value of the transaction was no more than \$30,000.

[Schedule 3, item 2, regulations 5.5.04(2) and (4)]

The effect of this is that, for transactions that occurred in the three months before the relation-back day, or after that day but before the winding up began, an unfair preference is only voidable in a simplified liquidation process if a creditor under the transaction was a related entity of the company and the value of the transaction was more than \$30,000.

The term ‘related entity’ in relation to a body corporate is defined in section 9 of the Corporations Act. The term captures a wide group of people and entities and is intended to facilitate the recovery of assets transferred to such entities under the voidable transaction provisions.

Provision for a series of transactions is intended to avoid misuse of the exemption where a transaction valued at more than \$30,000 is spread over a series of smaller payments. Such a series of related transactions does not fall within the exemption in regulation 5.5.04.

A transaction that does not meet the criteria described above may remain a voidable transaction and the liquidator may seek an order of the Court to have the transaction set aside. Also, where a liquidation ceases to follow the simplified liquidation process, a transaction that was not voidable because of the exemption in regulation 5.5.04 is no longer exempt, and the liquidator may seek an order of the Court to have the transaction set aside.

Reporting to ASIC

Reporting offences or other breaches

Under a general liquidation process, a liquidator is required to lodge a report to ASIC if it appears to the liquidator that a past or present officer or employee of the company is guilty of an offence, or if a person involved with the company may have appropriated company property or breached a duty, or if the company may be unable to pay its unsecured creditors more than 50 cents in the dollar. The purpose of this requirement is to ensure that ASIC is informed of potential misconduct of the company or its officers and to allow ASIC or the liquidator to take appropriate action. See section 533 of the Corporations Act.

Under the simplified liquidation process, the liquidator is not required to lodge a report with ASIC under section 533 of the Corporations Act (see section 500AE(2)(a) of the Corporations Act).

Instead, section 500AE(3)(f) of the Corporations Act enables the Corporations Regulations to prescribe information, reports and documents that are to be provided to ASIC in relation to a company under simplified liquidation. *[Schedule 3, item 2, regulation 5.5.05(1)]*

Accordingly, the Regulations insert regulation 5.5.05 to require that a liquidator must lodge a report where, in their opinion, there are reasonable grounds to believe that a person may have engaged in conduct constituting an offence under a law of the Commonwealth or a State or Territory in relation to the company that has had, or is likely to have, a material adverse effect on the interests of the creditors as a whole or of a class of creditors as a whole. A relevant person for the purposes of this test is a person who is a past or present officer or employee, or a member or contributory, of the company or a person who has taken part in the formation, promotion, administration, management or winding up of the company. What amounts to a material detriment to the creditor depends on the nature and circumstances of the conduct, the company and the creditor involved. *[Schedule 3, item 2, regulation 5.5.05(2)]*

The liquidator must lodge this report with ASIC as soon as practicable, or in any event, within six months after first forming the belief. *[Schedule 3, item 2, regulation 5.5.05(2)(c)]*

The report must:

- state whether the liquidator proposes to make an application for an examination or order under section 597 of the Corporations Act; and
- give ASIC such information, or give ASIC access to and facilities for inspecting and taking copies of any documents as ASIC requires.

[Schedule 3, item 2, regulations 5.5.05(2)(c) and (d)]

The Regulations empower a form to be prescribed for the report. If a form has been prescribed for this purpose, the liquidator must lodge the report in that form. Otherwise, if no form has been prescribed for this purpose, there is no particular form requirement and the report must be lodged in writing. *[Schedule 3, item 2, regulation 5.5.05(2)(c)]*

The liquidator may also lodge reports specifying any other matter that, in their opinion, it is desirable to bring to the notice of ASIC. *[Schedule 3, item 2, regulation 5.5.05(3)]*

Regulation 5.5.05 also prescribes a power for the Court to direct the liquidator to lodge a report (if the liquidator has not done so already) where it appears to the Court that:

- a past or present officer or employee, or a contributory or member, of the company has been guilty of an offence under a law of the Commonwealth or a State or Territory in relation to the company; or
- a person who has taken part in the formation, promotion, administration, management or winding up of the company may have misapplied or retained, or may have become liable or accountable for, any money or property of the company or may have been guilty of any negligence, default, breach of duty or breach of trust in relation to the company.

The Court's power to direct the liquidator in this way may be exercised on the application of a person interested in the winding up. *[Schedule 3, item 2, regulation 5.5.05(04)]*

This may include, for example, a creditor or member of the company subject to the simplified liquidation.

Reporting entry into and exit from the simplified liquidation process

A liquidator is required to notify ASIC when the liquidator:

- adopts the simplified liquidation process (under section 500A(1) of the Corporations Act); and
- ceases to use the simplified liquidation process (under section 500AC(1) of the Corporations Act).

[Schedule 3, item 2, regulations 5.5.06 and 5.5.08(2)]

The liquidator must notify ASIC within two business days after the adoption or cessation of the simplified liquidation process. The Regulations empower a form to be prescribed for the report. If a form has been prescribed for this purpose, the liquidator must lodge the report in that form. Otherwise, if no form has been prescribed for this purpose, there is no particular form requirement and the report must be lodged in writing. *[Schedule 3, item 2, regulations 5.5.06(2)(a) and 5.5.08(2)]*

When a liquidator adopts the simplified liquidation process, the liquidator must also lodge with ASIC a copy of the declaration given by the directors of the company to the liquidator in accordance with section 498 of the Corporations Act. *[Schedule 3, item 2, regulation 5.5.06(2)(b)]*

A liquidator's failure to comply with the requirement to notify ASIC is an offence. *[Schedule 3 item 2, regulations 5.5.06 and 5.5.08(2), and section 1311 of the Corporations Act]*

The imposition of an offence is necessary to ensure that liquidators report information to ASIC about the use of the simplified liquidation process, including when use of the simplified process has ceased. This information is necessary to enable ASIC to oversee the liquidation of companies using the simplified process. In this way, the imposition of an offence is intended to reduce the incidence of behaviour that would otherwise be prohibited by the Corporations Act.

Because no penalty is specified for the offence, the offence is an offence of strict liability and a registered liquidator who commits the offence may be punished on conviction with a penalty not exceeding 20 penalty units (see sections 1311A and 1311F of the Corporations Act). As a strict liability offence, no fault element applies to a liquidator's failure to give ASIC notice but the defence of mistake of fact is available. This is consistent with established principles in the Criminal Code as well as the existing legislative scheme for offences set out in Part 9.4 of the Corporations Act.

In considering the imposition of this offence, regard has been had to the Guide to Framing Commonwealth Offences.

Dividend process

Under a liquidation process, the liquidator is responsible for distributing any available funds to creditors in accordance with the priorities set out in the Corporations Act. This occurs when the liquidator has gathered enough funds to provide dividends to all creditors that prove their debt. To receive distributions, a creditor who has debts due against a company, or claims to a debt against a company must provide this information to the liquidator. This may be done either formally or informally as required by the liquidator in accordance with section 553D of the Corporations Act.

Proofs of debt and claims

Section 500AE(3)(c) of the Corporations Act empowers the Corporations Regulations to prescribe the process for proofs of debt and claims in relation to a company that is subject to the simplified liquidation process. Under the simplified liquidation process, the process for a creditor proving their debts and claims is generally the same as the regular liquidation process with some minor changes.

The Regulations provide that where a liquidator requires a debt with formal proof, the liquidator must provide the creditor with 14 days to submit their proofs of debt and claims, along with any particulars that substantiate the claim. The period of 14 days begins from when the notice to submit the particulars of a debt or claim are lodged with ASIC in accordance with regulation 5.6.39(2). This includes any detailed particulars of the claims or debts and, in the case of a debt, a statement of account and specifications of vouchers (if any) by which the statement can be substantiated (see regulation 5.6.50). *[Schedule 3, items 5 and 12, regulations 5.6.39 and 5.6.48(1)]*

The Regulations provide that the liquidator of a company may only call once for creditors to submit the particulars of their debts and claims. This differs from the regular process which allows the liquidator to call for creditors as many times as is necessary throughout the liquidation process. Where the liabilities exceed the threshold and the liquidator becomes aware of more complex debt arrangements, the liquidator will cease to use the simplified liquidation process and move into the regular liquidation process (further discussion below). *[Schedule 3, items 5 and 12, regulations 5.6.39 and 5.6.48(1)]*

The intention is that the simplified liquidation process be used by small companies with non-complex debt requirements. Given the threshold relating to the liabilities, it is unlikely that these companies will have large amounts of creditors that will be unknown to the company.

The liquidator also maintains the discretion to accept a debt without formal proof. If the liquidator does accept informal proof, the notification for submission of the claims by the liquidator as well as creditors rights are the same as the regular liquidation process. *[Schedule 3, item 9, regulation 5.6.39(4)]*

Once received, the liquidator must either choose to accept or reject the creditor's particulars. Similar to the regular liquidation process, the liquidator has 28 days to inform the creditor of the outcome of their debt or claim. The liquidator may admit all or part of the formal proof of debt or claim, reject all or part of it, or require further evidence in support of it (see regulation 5.6.53). The simplified liquidation process

retains all of the creditor's rights in relation to the proofs of debt and claims process. This includes the ability to amend a statement of claim where further information comes to light about the company's liabilities owed to the particular creditor. For example this may occur where there are other outstanding tax liabilities that come to light once the company enters the simplified liquidation process.

Declaring and distributing a dividend

Section 500AE(3)(e) of the Corporations Act provides that the Corporations Regulations may also provide for circumstances when a liquidator may declare and distribute a dividend.

Under the simplified liquidation process, a liquidator of a company may declare a dividend by lodging a notice with ASIC and notifying creditors that are known to the liquidator. The requirement in regulation 5.6.65 that the liquidator must not give notice of intention to declare a dividend not more than two months before the intended date does not apply in a simplified liquidation process. *[Schedule 3, item 18, regulation 5.6.65]*

The liquidator may only declare and distribute a dividend once among creditors whose debts or claims have been admitted. *[Schedule 3, item 19, regulation 5.6.67A]*

An expedited dividend process allows creditors to get paid quickly. This reflects the intention that the simplified liquidation process is efficient and is consistent with the recommendations from the Productivity Commission in its 2015 inquiry, entitled *Business Set-up, Transfer and Closure*.

Unlike under the regular liquidation process, a creditor who has not had their debt or claim admitted before the declaration of a dividend does not have a right to the distribution of a dividend. *[Schedule 3, item 20, regulation 5.6.68(3)]*

Although this impacts on a potential creditor's rights, this requirement ensures that the liquidation process remains cost and time efficient by encouraging all potential creditors to respond within the timeframes required by the liquidator.

Circumstances in which a liquidator must cease to follow the simplified process

Section 500AC(1)(b) of the Corporations Act empowers the Corporations Regulations to prescribe circumstances in which the liquidator of a company must cease to follow the simplified liquidation process.

The Regulations provide that the liquidator must cease to follow the process where the liquidator has reasonable grounds to believe that the company or a director of the company has engaged in conduct that has had or is likely to have, a material adverse effect on the interests of the creditors as a whole or of a class of creditors as a whole. What amounts to a material adverse effect depends on the nature and circumstances of the conduct, the company and the creditor involved. *[Schedule 3, item 2, regulation 5.5.07(1)]*

Further, the liquidator must have reasonable grounds to believe that the conduct was fraudulent or dishonest. This reflects the intention that only conduct that indicates to a liquidator that genuine misconduct or wrongdoing has occurred is intended to require the liquidator to cease to follow the simplified liquidation process. Conduct of the

nature in described by regulation 5.5.07 may indicate conduct, or the existence of further conduct, that should be subject to the comprehensive investigatory requirements of the regular liquidation process *[Schedule 3, item 2, regulation 5.5.07(1)]*

Example 1: Company engaging in dishonest conduct affecting creditors' interests

Bilby Pty Ltd is an entity within a closely held private group. Bilby entered into a creditors' voluntary liquidation and the liquidator subsequently adopted the simplified liquidation process.

In conducting the liquidation, the liquidator discovered that, over a period of time, there had been several changes to the directors of Bilby. There are indications that straw or dummy directors were used. Bilby's financial records, including records about company assets and the value of outbound transfers, are incomplete. Bilby had several years of outstanding tax lodgements which were only recently submitted. Bilby has significant dealings in cash receipts, and it appears its tax returns understate taxable income. Across the group there is a pattern of liquidations.

Based on these facts, the liquidator forms a reasonable belief that Bilby and its directors engaged in conduct that involved fraud and dishonesty and which likely had a material adverse effect on the interests of creditors as a whole. The liquidator must cease to follow the simplified liquidation process for Bilby and, under the regular liquidation process, may need to make a report about the conduct under section 533 of the Corporations Act.

The Regulations provide that the liquidator is taken to have ceased to follow the simplified liquidation process on the day on which the liquidator first held the belief that the conduct has been engaged in. *[Schedule 3, item 2, regulation 5.5.07(2)]*

Transition from the simplified liquidation process

Section 500AC(2) of the Corporations Act empowers the Corporations Regulations to deal with the transition from a simplified liquidation process to another form of external administration.

The Regulations provide that the cessation of the simplified liquidation process in relation to a company does not affect the validity of anything that was done in good faith in relation to the company before the cessation. *[Schedule 3, item 2, regulation 5.5.08(3)]*

Further, where a liquidation moves from the simplified to the regular liquidation process, a liquidator may need to provide a report to ASIC under section 533 of the Corporations Act regarding a circumstance that was not required to be reported under the simplified liquidation process. In this circumstances, the liquidator must provide the report within six months after the day on which the simplified liquidation process in relation to the company ended. *[Schedule 3, item 2, regulation 5.5.08(4)]*

Minor and consequential amendments

The Regulations make a number of minor and consequential amendments to insert a new division heading in Part 5.5 of the Corporations Regulations and new subheadings and cross-references relevant to the proof of dividend process in regulations 5.6.39 and 5.6.48. *[Schedule 3, items 1, 3, 4, 6 to 8, 10, 11 and 13 to 17, regulations 5.6.39 and 5.6.48]*

Application of amendments

The amendments made by the Regulations for the simplified liquidation process apply in relation to the winding up of a company that began because of a triggering event that occurs on or after the commencement of the amendments to the Corporations Act that creates the simplified process. *[Schedule 3, item 21, regulation 10.43.01]*

Schedule 4 – Amendments relating to electronic communication of documents

Regulation 5.6.11A is repealed. Formerly, this provision allowed documents relating to an external administration required or permitted to be given under certain provisions of the Corporations Regulations to be given using electronic means as nominated by the recipient. Giving documents electronically under the Corporations Regulations is now governed by the facilitative rules in section 600G of the Corporations Act. Accordingly, regulation 5.6.11A is no longer necessary and is repealed. *[Schedule 4, item 1, regulation 5.6.11A]*

Formerly, notes were required to identify the small subset of provisions where the requirements to give a document could be satisfied by using electronic means under the former regulation 5.6.11A. However, the new facilitative rules that provide for the use of electronic communication are much broader in scope than the former rules and apply to all documents provided under Chapter 5 of the Corporations Regulations.

Accordingly, the notes are no longer needed and are repealed. *[Schedule 4, items 2-10, the note to subregulation 5.6.48(2), the note to subregulation 5.6.53(1), the note to subregulation 5.6.54(1), the note to subregulation 5.6.55(3), the note to subregulation 5.6.59(1), the note to subregulation 5.6.62(1), the note to subregulation 5.6.65(1), the note to subregulation 5.6.66(1), the note to subregulation 5.6.66(3)]*

Regulation 5.6.11A(6) is likewise repealed. This provision contained a cross-reference to the definition of ‘electronic communication’ in section 5(1) of the *Electronic Transactions Act 1999*. Section 9 of the Corporations Act contains a definition of ‘electronic communication’ mirroring that definition. Accordingly, the cross-reference is not required. *[Schedule 4, item 11, subregulation 5.6.75(6)]*

Schedule 5 – Amendments to the Corporations (Fees) Regulations 2001

Schedule 5 makes amendments to the *Corporation (Fees) Regulations 2001* (the Fees Regulations) to temporarily waive the fees associated with registration of a registered liquidator for the period 1 January 2021 to 30 June 2022.

The Fees Regulations specify the fees imposed for chargeable matters that occur under the Corporations Act (see section 5 of the *Corporations (Fees) Act 2001*).

In this Schedule, legislative references are to the Fees Regulations unless otherwise specified.

Temporary waiver for liquidator fees – 1 January 2021 to 30 June 2022

Schedule 1 sets out regulatory fees for chargeable matters under the Corporations Act.

The Regulations amend item 12 of the table in Schedule 1 to prescribe that there is no fee for an application under section 20-5 of the Insolvency Practice Schedule for registration as a liquidator. However, this is the case only if the application is the first application lodged by the applicant in a calendar year. For example, if a person applies for registration as a registered liquidator, and is rejected, the Regulations provide that a person who lodges another application of the same kind within the same calendar year must pay a fee of \$2,200. *[Schedule 5, item 1, item 12 of the table in Schedule 1]*

The Regulations also amend item 13 of the table in Schedule 1 to prescribe that there is no fee for the registration by ASIC of a person as a liquidator under section 20-30 of the Insolvency Practice Schedule. *[Schedule 5, item 2, item 13 of the table in Schedule 1]*

The temporary waiver of fees associated with registration of a liquidator is intended to encourage more practitioners to enter or re-enter the external administration sector. The amendments to the Fees Regulations, along with the amendments to the registration of insolvency practitioners in the Insolvency Practice Rules and the temporary relief measures in Schedule 2 to the Regulations, assists in expanding the availability of insolvency practitioners to deal with the expected increase in the number of businesses seeking to restructure or liquidate following the commencement of the new debt restructuring and simplified liquidation processes.

Return to regular liquidator fees – from 1 July 2022

The prescription of no fee for an application under section 20-5 of the Insolvency Practice Schedule for registration as a liquidator and for the registration by ASIC of a person as a liquidator under section 20-30 of the Insolvency Practice Schedule applies in the period 1 January 2021 to 30 June 2022. Starting on 1 July 2022, items 12 and 13 of the table in Schedule 1 are amended so that the fees revert to previous prescribed fee amounts of \$2,200 and \$1,300 respectively. *[Schedule 5, items 3 and 4, items 12 and 13 of the table in Schedule 1]*

Other fees

Item 86 of the table in Schedule 1 prescribes a fee in relation to applying for ASIC to give a direction under section 448C(3)(b) of the Corporations Act (relating to the disqualification of a person from being appointed as administrator of a company or of a deed of company arrangement). The equivalent provision under the formal debt restructuring process is section 456C of the Corporations Act. This section enables ASIC to, if it thinks fit in the circumstances of the case, direct that a person is not to be taken as a director, secretary, senior manager, employee or auditor for the purposes of section 456C of the Corporations Act. The effect of such a direction is that, without requiring leave of the Court, a person may seek or consent to be appointed as a restructuring practitioner for a company or for a restructuring plan.

Consistent with the treatment of the equivalent chargeable event in section 448C(3)(b), the Regulations prescribe a fee of \$156 on application for ASIC to give a direction under section 456C(4)(b). *[Schedule 5, item 3, item 86A of the table in Schedule 1 to the Corporation (Fees) Regulations 2001]*

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020

The *Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020* (the Regulations) are compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Regulations

The Regulations amend the *Corporations Regulations 2001* (the Corporations Regulations) and the *Corporations (Fees) Regulations 2001* (the Fees Regulations) to enable the new debt restructuring and simplified liquidation regimes established by the *Corporations Amendment (Corporate Insolvency Reforms) Act 2020* (Insolvency Reforms Act). The Regulations also make further consequential amendments to the Corporations Regulations that are required as a result of the Insolvency Reforms Act.

Human rights implications

The Regulations engage, or may engage, the following applicable rights or freedoms:

- Article 14(2) of the International Covenant on Civil and Political Rights (ICCPR) (presumption of innocence); and
- Article 17 of the ICCPR (right to privacy and reputation).

In assessing the impact on human rights, consideration has been given to the Parliamentary Joint Committee on Human Rights' Guidance Note 2: Offence provisions, civil penalties and human rights (Guidance Note 2), and the Attorney-General's Department's *A Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*, September 2011 edition (the Guide to Framing Commonwealth Offences).

Strict liability offences

Article 14(2) of the ICCPR provides that everyone charged with a criminal offence has the right to be presumed innocent until proven guilty. Generally, consistency with the presumption of innocence requires the prosecution to prove each element of a criminal offence beyond reasonable doubt. The effect of applying strict liability to an element of an offence means that no fault element needs to be proven by the prosecution, although the defence of mistake of fact is available to the defendant. This may have the effect of limiting an individual's right to a fair trial.

Consistent with Guidance Note 2, strict liability and absolute liability offences will not necessarily be inconsistent with the presumption of innocence provided that they

are within reasonable limits, taking into account the importance of the objective sought to be achieved, and maintain the defendant's right to a defence. In other words, such offences must pursue a legitimate objective and be rationally connected and proportionate to that objective.

Schedules 1 and 2 to the Regulations contain strict liability offences that apply to individuals. In particular, the following types of offences are provided in Schedule 1:

- where the small business restructuring practitioner fails to make reasonable inquiries into, and take reasonable steps to verify the company's business, property, affairs and financial circumstances before certifying the proposed restructuring plan (regulation 5.3B.16);
- where the small business restructuring practitioner fails to provide notification to the company that the practitioner has become aware of information contained in the plan or the restructuring proposal statement that is incomplete or inaccurate, and believes this is likely to affect the company's ability to meet its obligations under the restructuring plan (regulation 5.3B.17);
- where a person gives, agrees or offers to give, any valuable consideration to an affected creditor with the intention of affecting the acceptance or rejection of the proposed restructuring plan (regulation 5.3B.23).

Schedule 2 also provides an offence where a liquidator fails to notify ASIC within five business days of the adoption or cessation of the simplified liquidation process (regulations 5.5.06 and 5.5.08).

These offences are appropriate to achieve the legitimate objective of reducing non-compliance with the new debt restructuring and simplified liquidation processes, therefore maintaining the integrity of the external administration regime.

The offences contained in Schedule 1 are rationally connected to the legitimate objective by incentivising all parties to the restructuring plan to adhere to the obligations imposed on them as well as preventing any potential misuse of the debt restructuring process.

The offence contained in Schedule 2 is rationally connected to the legitimate objective by ensuring that the liquidator fulfils their notification requirements to ASIC which assists ASIC in their regulatory responsibilities.

In addition to this, the strict liability offences are proportionate as the offences have been made with regard to the Guide to Framing Commonwealth Offences. These offences are consistent with these requirements as the offences are not punishable by imprisonment and the fines do not exceed 60 penalty units.

Furthermore, the strict liability offences also preserve the defence of honest and reasonable mistake of fact to be proved by the accused on the balance of probabilities. This defence maintains adequate checks and balances for persons who may be accused of such offences.

To the extent that the Regulations engages the right under Article 14(2) of the ICCPR, it is compatible with human rights as the strict liability offences are appropriate and consistent with the requirements of the Guide to Framing Commonwealth Offences.

Right to privacy and reputation

Schedules 1 and 2 to the Regulations contain reporting requirements that may require information to be shared with creditors and ASIC that includes personal information. In addition to this, Schedule 1 contains a qualified privilege defence for defamation proceedings against the small business restructuring practitioner.

Provisions in the Regulations may, or may not, engage Article 17 of the ICCPR which protects an individual's right to of privacy and reputation. The following provisions are contained Schedule 1:

- where the small business restructuring practitioner for the company or the plan has qualified privilege for any statement they have made in the performing or exercising of their functions and powers (regulations 5.3B.09 and 5.3B.36);
- where the small business restructuring practitioner has to notify and lodge their name and contact details with ASIC upon their appointment and upon the termination of the restructuring process (regulations 5.3B.45 and 5.3B.06).

Schedule 2 also provides that where a liquidator has in their opinion, reasonable grounds to believe that a person connected with the company may have engaged in conduct that is an offence under the law and that is or may have a material adverse effect on the interests of creditors, they need to report this to ASIC and give ASIC such information as it requires (regulations 5.5.05 and 5.5.08(4)).

Right to privacy

Article 17(1) of the ICCPR provides that no one shall be subjected to arbitrary or unlawful interference with his or her privacy, family, home or correspondence, nor to unlawful attacks on their honour and reputation.

The right in Article 17 may be subject to permissible limitations, where these limitations are authorised by law and are not arbitrary. In order for an interference with the right to privacy to be permissible, the interference must be authorised by law, be for a reason consistent with the ICCPR and be reasonable in the particular circumstances.

The UN Human Rights Committee has interpreted the requirement of 'reasonableness' to imply that any interference with privacy must be proportional to the end sought and be necessary in the circumstances of any given case.

Under the Regulations, the small business restructuring practitioner and the liquidator must, in certain circumstances, lodge information with ASIC. This may engage the right to privacy, to the extent that it includes the disclosure of personal or confidential information.

In Schedule 1 to the Regulations, the practitioner must lodge information with ASIC upon their appointment and upon the termination of restructuring process. These

notice requirements may engage the right to privacy, to the extent that this information includes personal information relating to the small business restructuring practitioner. However, these notices are already required by existing provisions in the Corporations Act. This is because the notice requirements in the new debt restructuring process replicate existing information reporting requirements in other external administration processes in the Corporations Regulations. The replication of these requirements provides consistency between the new debt restructuring process and the existing external administration regime.

In Schedule 2 to the Regulations, regulations 5.5.05 and 5.5.08 require that the liquidator must lodge a report with ASIC where, in the liquidator's opinion, there are reasonable grounds to believe that a person may have engaged in conduct constituting an offence under a law of the Commonwealth or a State or Territory in relation to the company that has had, or is likely to have, a material adverse effect on the interests of the creditors as a whole or of a class of creditors as a whole. This may engage the right to privacy, to the extent that this information may include personal information about a relevant person.

A relevant person for the purposes of this test is a person who is a past or present officer or employee, or a member or contributory, of the company or a person who has taken part in the formation, promotion, administration, management or winding up of the company.

The sharing of this information with ASIC is important to assist with ASIC's investigation and enforcement functions. It alerts the regulator to any potential offences that may have occurred by the relevant person. This achieves the legitimate objective of maintaining the compliance with the corporate insolvency regime and enables better monitoring of illegal and other high-risk activities by the regulator.

In addition to the above, any information that is provided by the small business restructuring practitioner or the liquidator to ASIC will remain subject to strict confidentiality protections. When information is shared with ASIC and that information contains personal information about an individual, ASIC must comply with disclosure and retention principles contained in the *Privacy Act 1988*. This information is also received as 'protected information' under section 127 of the *Australian Securities and Investments Act 2001*, which prohibits disclosure and unauthorised use unless in specified circumstances.

To the extent that the Regulations engage the rights under Article 17(1) of the ICCPR, this is proportionate and limited to achieving the legitimate objective.

Right to the protection of the law against interference or attacks against a person's reputation

Article 17(2) of the ICCPR provides that a person has the right to the protection of the law against interference or attacks of a person's privacy, family, home and correspondence.

The Regulations promote Article 17(2) of the ICCPR by providing protection for a restructuring practitioner to defend themselves against allegations about their reputation.

In particular, regulations 5.3B.09 and 5.3B.36 provide the small business restructuring practitioner for the company or the plan with qualified privilege for any statement they have made in good faith and without negligence, in the performance or in the exercising of their functions and powers. This provides a lawful defence for defamation allegations against any correspondence of the small business restructuring practitioner.

In this way, the Regulations promote Article 17(2) of the ICCPR by providing important safeguards to allow practitioners the ability to undertake their functions, including investigating and reporting on the affairs of the company, without risk of legal proceedings.

Conclusion

To the extent that Schedules 1 and 2 engage Articles 14 and 17 of the ICCPR, the engagement of the applicable rights and freedoms, is reasonable, necessary and proportionate.

Schedules 3, 4 and 5 are compatible with human rights obligations as they do not raise any human rights issue.

**Regulation Impact Statement –
Insolvency reforms to support small business**

Background

Recent evaluations of the Australian corporate insolvency framework, including by the Productivity Commission in 2015¹, have confirmed that it performs well on most fundamental indicators, including the time taken during an insolvency process, the proportion of funds recovered, creditor participation and the management of debtor assets.

But significant issues with the framework have still been identified. One issue that has been raised consistently – by government agencies, stakeholder groups and international bodies – is the failure of the Australian system to account for the needs and characteristics of different size businesses during insolvency, particularly small business.

In corporate insolvency, Australia has a one-size-fits-all system, which simultaneously must account for the needs of all business types. In practice, this means that key components of our laws have been designed to respond to the complexity of a large corporation. The Australian Restructuring Insolvency and Turnaround Association (ARITA) has previously advocated for the need to streamline the current insolvency processes for small businesses. In 2020, the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) in its *Insolvency Inquiry Report* also recommended the Government adopt streamlined insolvency processes for small businesses and argued the current regime was not working for small businesses.² The ASBFEO stated:

Small business owners report facing an opaque system, where decisions are taken out of their hands, they feel pushed into outcomes they were not looking for, and their expertise or knowledge of the business they have been running is discounted or ignored.

International organisations have also recognised the issues posed by a one size fits all approach. The Organisation for Economic Co-operation and Development (OECD), for example, found in its Going for Growth report³ that:

Small and medium enterprises (SMEs) may warrant a different treatment from other firms in a debt restructuring strategy as complex, lengthy and rigid procedures, as well as required expertise and high costs of insolvency can fail to adequately meet the needs of SMEs.

Special insolvency procedures for SMEs... could ensure that non-viable ones exit and viable ones in temporary distress are restructured without delay.

As a part of the Government's response to COVID-19 [temporary relief for financially distressed businesses](#) was introduced through the *Coronavirus Economic Response*

¹ Productivity Commission 2015, 'Business Set-up, Transfer and Closure: Productivity Commission Inquiry Report', <https://www.pc.gov.au/inquiries/completed/business/report/business.pdf>

² ASBFEO 2020, Insolvency Practices Inquiry: Final Report <https://www.asbfeo.gov.au/sites/default/files/Insolvency%20Inquiry%20Final%20Report.pdf>

³ OECD 2018, 'Going for Growth', p.97, <http://www.oecd.org/economy/growth/policies-for-productivity-the-design-of-insolvency-regimes-across-countries-2018-going-for-growth.pdf>

Package Omnibus Act 2020 which received Royal Assent on 24 March 2020. The relief increased the minimum threshold for creditors issuing a statutory demand from \$2,000 to \$20,000 and increased the time to respond to the statutory demand from 21 days to six months. Directors were also given temporary relief from personal liability if a company trades while insolvent. The Treasurer was also granted instrument-making power to make temporary amendments to the *Corporations Act 2001* (the Corporations Act). These temporary changes were scheduled to apply for 6 months, from 25 March 2020 until 24 September 2020. On 7 September 2020, the Treasurer [announced](#) that the temporary insolvency measures would be extended until 31 December 2020.

The removal of the temporary insolvency protections will have an impact on the number of companies entering external administration due to the effectiveness of measures in keeping firms out of external administration due to the impacts of COVID-19. This risks a ‘wave’ of external administrations occurring in the lead up to and immediately following the winding back of temporary support measures. From April to September 2020, there was a decrease in companies entering external administration of 51.2 per cent compared to the same period in 2019 (a decrease from 4,404 to 2,139). Extrapolating this rate to the end of the year results in approximately 3,000 companies that have not entered external administration compared to the corresponding period last year.

Following the implementation of the temporary insolvency measures, Treasury undertook consultation with stakeholders to gauge their impact and effectiveness, and test the case for any further government action. Treasury held regular meetings with stakeholders including ARITA, the Turnaround Management Association (TMA), and other stakeholder groups. These meetings helped Treasury to understand the impact of the temporary measures and the broader effectiveness of the current insolvency framework in light of the impact of COVID-19. Treasury also met with the ASBFEO to discuss the findings of its insolvency practices inquiry in the context of COVID.

In these consultations stakeholders also repeated concerns on the need for a small business regime, and argued that the pressures that COVID-19 has placed on business and the insolvency sector have made the case for permanent reform of the insolvency framework more urgent.

The lack of technological neutrality surrounding the external administration provisions of the Corporations Act has also been a concern for industry due to the resulting regulatory burden. This includes requirements to provide notice documents in hard copy by post, and to hold meetings in physical locations (even if participants would prefer to attend virtually).

On 6 May 2020, the Treasurer made a determination under the temporary instrument-making power that was inserted in the Corporations Act as part of the Government’s Coronavirus economic response package. The determination provides temporary relief by allowing companies and insolvency practitioners to virtually or electronically satisfy requirements related to their legal obligations concerning meetings and document execution. This supported them to continue operating while still meeting social distancing requirements imposed as a result of the continuing uncertainty caused by COVID-19.

The temporary relief has also provided an opportunity to test with stakeholders how making these requirements technologically neutral operates in practice to deliver options for companies to meet their obligations under the Corporations Act. This has provided an opportunity to test the reforms and receive feedback on the lived-experience from stakeholders, companies and insolvency practitioners, on how the relief has been operating in practice.

1. What is the policy problem you are trying to solve?

Importance of an insolvency system

An efficient and effective insolvency system is important in generating business dynamism, which is needed to underpin our economic recovery. The system helps the movement of capital and jobs to more productive from less productive firms. It allows the efficient winding up of businesses, ensuring creditors and employees are paid fairly.

Insolvency affects a large number of businesses, with ASIC data showing that 8,105 companies entered external administration⁴ in 2018-19.⁵ Behind these companies sit a larger number of affected creditors, business owners and employees. Of these 8,105 companies, only 1,226 entered voluntary administration. The pool of practitioners to manage these external administrations is also comparatively small: there were only 648 Registered Liquidators in 2018-19.

The effectiveness and efficiency of our insolvency system is very important for small businesses. Most of the companies which interact with the insolvency system are small businesses. According to ASIC data, around 76 per cent of companies entering into external administration in 2018-19 had less than \$1 million in liabilities. Of these, around 98 per cent are estimated to be businesses with less than 20 full-time equivalent employees.⁶

Issues with Australia's insolvency framework

Australia's insolvency framework is failing to fully accommodate the needs of Australian small businesses. The issues include:

- The need to ensure that regulatory obligations are commensurate with the complexity of the business and the likelihood of misconduct.
- The need to maximise the opportunity for distressed but viable companies to restructure and survive.
- The need to maximise returns for creditors in the event that a business is wound up.

Currently, Australian businesses can only access insolvency processes that are the same no matter the size of the business. As outlined below, the current processes are

⁴ A term used to describe one of the formal insolvency processes.

⁵ ASIC 2020, Australian insolvency statistics, <https://download.asic.gov.au/media/5841015/asic-insolvency-statistics-series-2-published-november-2020.pdf>

⁶ ASIC 2020, Australian insolvency statistics

better suited to larger, more complex company failure, which may have greater means to engage in sophisticated forms of misconduct.

However, most companies engaging with these processes are smaller companies who overwhelmingly fail ‘honestly’. In these cases, the current requirements are not proportionate to the size and complexity of the company, and to the assets or liabilities that they hold. As ASIC, in its submission to the 2015 Productivity Commission review on Business Set-up, Transfer and Closure⁷, stated:

Current insolvency laws take a, ‘one size fits all’ approach; with the same duties and obligations imposed on the external administrator [a broad category of insolvency practitioner, including liquidators] regardless of the size and complexity of the external administration.

Industry has argued that the cost of administering small- to medium- size enterprises is high and often the external administrator is required by current law to undertake tasks (investigations and reporting to creditors and ASIC) in circumstances where there are insufficient assets to pay the costs of this work.

This state of affairs has significant repercussions for Australian businesses, especially small business:

- It imposes costs across all parties involved in dealing with an insolvent business. In most cases, businesses are required to enter an insolvency process once they become insolvent. Inefficiencies in the insolvency processes mean reduced returns for creditors, and less money to reinvest in other activities.
- High costs, complexity and other factors can discourage businesses, especially small businesses, from entering into insolvency processes early when they have more chance at successful restructure, or more assets to distribute to creditors.

Facilitating restructure

Organisations including the OECD have stated that the first priority of an insolvency system should be to enable companies that are distressed but ultimately viable to restructure.⁸ Doing so allows the company to continue to compete in the market in a more efficient form, preserving business value and employee linkages.

Despite this, there are significant limitations to voluntary administration, the main formal insolvency process aimed at enabling insolvent companies to restructure:

- Voluntary administration tends to be a high-cost process. It requires an administrator to take on liability for debts incurred by the company, which the administrator must indemnify themselves against.

⁷ ASIC 2015, Productivity Commission: Review of Barriers to Business Entries and Exits in the Australian Economy, p. 39, <https://www.aph.gov.au/DocumentStore.ashx?id=011ea16b-b0f5-4a57-8c5a-7a26b40acbb8&subId=401940>

⁸ OECD 2018, ‘Going for Growth’, p.91.

- It provides very broad powers to the administrator, who take on the running of the company during voluntary administration. In turn, this means more rigorous registration requirements must be applied for administrators which reflect the complexity of the process.
- It requires an external administrator to take over the running of a company and the risks of trading (subject to an indemnity), which may discourage use of the process and the continued trading of the business when it is used.

These factors may limit the usefulness of voluntary administration for small businesses especially. For small businesses, the high costs of voluntary administration can also consume most or all of the value of a small business's assets, making successful restructure difficult. The powers and expertise of an administrator for a large firm may not be in line with the needs of a distressed small business (who may simply need an avenue to pay down an outstanding debt). Small and family businesses may be especially reluctant to call in an external administrator to take over the running of a company, reducing the opportunity for a company to restructure early when it is more likely to be viable.

Stakeholders have proposed alternative policies to address the limitations of voluntary administration as a small business restructuring tool. For example, ARITA in 2015 proposed a simplified debt restructuring process for 'micro' companies⁹. The OECD also encouraged Australia to adopt a debt restructuring strategy for SMEs which applied different treatment for smaller firms, with the intent of reducing the barriers associated with "complex, lengthy and rigid procedures, as well as required expertise and high costs."¹⁰

Liquidation

The current requirements imposed during a liquidation can require a stringent process which can be lengthy and expensive. Many of the current requirements imposed are aimed at detecting and addressing any misconduct that might have occurred in the lead up to insolvency. These include investigative requirements (behaviour that the insolvency practitioner must look for), requirements to call meetings (to seek creditor views and input on aspects of the process) and reporting functions (particularly to ASIC). Consequently, according to industry, even non-complex liquidations can take up to a year to complete.¹¹

While these requirements are appropriate for larger, more complex firms, the current requirements do not consider the needs of small business and the circumstances surrounding most small business insolvencies. According to ASIC administrative data, the vast majority of insolvencies in Australia are small businesses. These businesses overwhelmingly 'failed honestly'. That is, most businesses failed because of factors like inadequate cash flow, trading losses or economic conditions, low sales, or increased competition, not because of intentional wrongdoing on the part of their

⁹ ARITA 2015, Submission to Productivity Commission review on Business Set-up, Transfer and Closure, p. 15 <https://www.arita.com.au/documents/pc-submission-020315-website.pdf>

¹⁰ OECD 2018, 'Going for Growth', p.97, <http://www.oecd.org/economy/growth/policies-for-productivity-the-design-of-insolvency-regimes-across-countries-2018-going-for-growth.pdf>

¹¹ Sewell and Kettle 2020, Liquidation, <https://sklawyers.com.au/faq/how-long-does-a-liquidation-last/>

directors. Indeed, ASIC data from 2006-2015 shows that, when accounting for reasons companies have failed (as identified by practitioners), fraud ranks tenth (just above companies that have failed due to natural disasters).¹²

By imposing the same requirements in every liquidation, our current system therefore risks imposing unnecessarily high regulatory impact on distressed small businesses. This has the effect of depleting their very limited asset base and reducing returns for creditors and employees. It is an efficient means of targeting and preventing misconduct like illegal phoenixing.¹³

Insolvency sector capacity

These issues are exacerbated given the significant economic impacts of COVID-19, which means their impact will be felt more acutely. The need for efficient processes that effectively meet the needs of companies is increased as a larger number of companies are expected to enter external administration over a short period as temporary support measures are wound back. As mentioned in the Background, from April to September 2020, there was a decrease in companies entering external administration of 51.2 per cent compared to the same period in 2019 (a decrease from 4,404 to 2,139). This decrease has been reasonably consistent across industries. Some notable examples include: construction that had a decrease of 60 per cent, retail trade that had a decrease of 42 per cent and accommodation & food services that had a decrease of 50 per cent. It is expected that the vast majority of these companies are small businesses.

In the absence of reforms, this may place significant pressure on our insolvency system. The approximately 3,000 companies that have deferred entering external administration will likely have to be processed by the insolvency sector following the winding back of temporary support as will other companies that have been severely impacted by COVID-19. There is currently no mechanism that allows for these external administrations to be spread over time.

The number of Registered Liquidators has steadily been decreasing in line with stagnating numbers of external administrations. In March 2017 there was 726 Registered Liquidators, which has now decreased to around 640. This body of practitioners may have been able to respond to market conditions to date. However the impacts of COVID-19 and the temporary insolvency relief, which have deferred a number of insolvencies, means that it is prudent to put in place measures to manage this potential shock.

¹² Productivity Commission 2015, 'Business Set-up, Transfer and Closure: Productivity Commission Inquiry Report', p. 75.

¹³ Illegal phoenixing occurs when a company is liquidated, wound up or abandoned to avoid paying its debts. A new company is then started to continue the same business activities without the debt. On 5 February 2020, the Government passed legislation to implement a suite of reforms to the corporations and tax laws to combat illegal phoenixing. The legislation helps the Australian Taxation Office (ATO) crack down on those who conduct or facilitate illegal phoenix behaviour. The Australian Securities and Investments Commission (ASIC) can now pursue new civil and criminal offences against those who promote or engage in illegal phoenixing. ASIC and liquidators have additional powers aimed at recovering assets for the benefit of employees and other creditors.

Furthermore, there are barriers to entry for new or returning insolvency practitioners that will also be reduced by adding flexibility to the legislative requirements that are used by ASIC, through the Insolvency Practitioner Registration and Disciplinary Committees, to assess new applicants. There are currently a range of prescribed conditions including that the insolvency practitioner must have 4,000 hours of relevant employment (which must fit into certain categories) at a senior level during the preceding 5 years. Although there is a provision that allows a Committee to register an insolvency practitioner that does not meet all of the prescribed conditions, it requires them to be registered with conditions specified by the Committee. In practice it may be difficult for the Committee to come up with suitable conditions. These barriers disproportionately impact women who are more likely to take a break in their career.

The lack of technological neutrality surrounding the external administration provisions of the Corporations Act has also been a concern for industry due in part to the resulting regulatory burden. This includes requirements to provide notice documents in hard copy by post, and to hold meetings in physical locations (even if participants would prefer to attend virtually).

2. Why is government action needed?

While many factors impact the efficiency of markets, an insolvency system performs an important function in this regard. The government is responsible for establishing and overseeing the system. In doing so, the government establishes the ‘rules of the game’ in the event of business failure, providing certainty to investors, and thereby facilitating access to credit.

Because government sets clear rules, creditors can have the confidence to lend to a business, with the certainty that a known process will follow if that business fails. For example, the system provides creditors with the rules that will determine the amount they will recoup if a debtor company fails. Clear and fair rules in this regard apply equal treatment to creditors from the same class, and promote an orderly winding up and distribution of remaining funds in liquidation while identifying and deterring creditor defeating misconduct (such as illegal phoenixing). However, an efficient insolvency system should also provide distressed but viable businesses the opportunity to restructure and to continue to trade to the benefit of the business, its creditors and employees, and the economy more generally.

In setting these rules, governments must carefully balance several objectives, all of which an insolvency framework seeks to achieve. These include:

- allowing inefficient and poorly performing firms to exit the market in an efficient and orderly manner.
- providing an opportunity for financially distressed but viable companies to restructure and reorganise their affairs.
- promoting investor confidence through enabling a system that identifies and deters wrongdoing.

It is important that governments consider how their insolvency frameworks are meeting these objectives, and whether they are appropriately balanced.

Small business restructuring and liquidation

Reforms to the Australian insolvency system would enable it to better meet these objectives, and in doing so, support more Australian business and the broader economy.

Government action is required to meaningfully effect change. The current regulatory settings are imposed by Government legislation and as such Government action is required. Furthermore, Government is well placed to include safeguards to protect against instances of misconduct.

Providing a bespoke process targeted at small business restructure will enable Australia's insolvency framework to better meet the objective of enabling viable companies to turnaround their affairs and to continue to operate in the market. It would address many of the shortcomings of voluntary administration, particularly regarding use of this process by small business. In doing so, it would encourage more small businesses to enter into restructuring early, rather than waiting until liquidation is the only option.

A simplified restructuring process would achieve these objectives by:

- Providing a process that is simpler and more easily understood.
- Allowing for lower costs, by reducing complexity and simplifying the role of the insolvency practitioner.
- Enabling a 'debtor-in-possession' model, which allows the business owners to remain in control of the company during the process (thereby reducing their reluctance to engage with the process and supporting the continued trading of the business during the process).

Likewise, a simplified liquidation process targeted at insolvent small businesses would allow unviable businesses to be wound up efficiently and cost effectively. This would be achieved by removing unnecessary or disproportionate obligations that the current liquidation process imposes on the insolvent business and its liquidator. These obligations relate to the level of investigation and reporting required, the ability to convene meetings and the ability to appoint reviewing liquidators and committees of inspections. Tailoring the liquidation process to the small business will ensure that more of the company's remaining assets are available for distribution to its creditors and employees, rather than being used to fund obligations imposed by the process itself.

Both of the above proposals would ensure our insolvency system could continue to meet the objective of identifying and preventing misconduct through appropriate enforcement. They would include safeguards which, as opposed to blanket obligations, are targeted to enable the processes to be used by honest firms, but prevent their use and reuse to facilitate misconduct like illegal phoenixing.

The safeguards include:

- The same company or directors using the process would be prohibited from using the process more than once within a prescribed period (proposed at 7 years).
- Both processes would retain an independent practitioner, who would administer them. They would retain obligations they must fulfil on behalf of creditors, as well as the power to end the process in appropriate circumstances.
- Related creditors would be unable to vote on a restructuring plan.

Increasing the capacity of the insolvency sector

While the simplified liquidation and restructuring processes will reduce the complexities and costs associated with external administration processes for many businesses, additional measures to ensure adequate capacity in the insolvency sector are needed to fully realise the benefits these processes can deliver. Specifically, it will be important to ensure a functional, competitive insolvency system so that the system can handle an increased number of external administrations and to encourage cost savings from simplified external administrations.

There are also barriers to achieving efficient technological neutral outcomes as result of the Corporations Act requirements in respect of meetings, meeting communications and other communications with creditors. Current barriers include requirements to provide notice documents in hard copy by post, and to hold meetings in physical locations (even if participants would prefer to attend virtually). These barriers reduce the ability of insolvency practitioners to fully utilise electronic means and other alternative technologies to comply with their obligations. This adds to the costs of external administration as more traditional approaches (in-person meetings and posting of hard copy materials) are more expensive, and often slower and unnecessary.

3. What policy options are you considering?

Without law reform, when the temporary relief expires, small incorporated businesses and the insolvency sector will be required to adhere to the requirements of the insolvency framework that were in place prior to the temporary relief. With a view to simplifying and streamlining the liquidation and reorganisation process going forward, the following options are being considered:

1. Allow the temporary relief to expire (on 31 December 2020) without permanent law reform (maintain the status quo)
2. Introduce simplified insolvency processes for small businesses (based on a company's liabilities being below \$1,000,000 when the process commences)¹⁴ and improve the capacity of the insolvency sector

¹⁴ Liabilities would be calculated so that it encompasses a broad range of liabilities incurred by the company.

3. Introduce simplified insolvency processes for small businesses (based on small businesses being eligible under a current legislative definitions of small businesses¹⁵) and improve the capacity of the insolvency sector

Option 1 – Status quo

The status quo could be maintained by retaining the current framework for liquidation and voluntary administration for businesses of all sizes.

Voluntary administration would remain the primary formal business restructure tool for insolvent businesses, including small businesses. Business owners seeking to use this process would have to assent to have an independent administrator to manage the business during the administration. The owner would have broad powers over the running of the business, and would be required to take on personal liability for the company.

For businesses seeking to wind-up, including small businesses, would have access to one liquidation process. Full investigatory, meeting and reporting requirements would apply to all companies seeking to access the process, regardless of the complexity of the insolvency or the risk that it has engaged in misconduct. For example:

- A liquidator may convene a meeting of creditors at any time.
- Creditors of a company in liquidation may decide that there is to be a committee of inspection (described below) to monitor the liquidation and to give assistance to the liquidator.
- Liquidators can continue to pursue unfair preference payments¹⁶ against unsecured creditors if the transaction occurred within 6 months prior to the 'relation back day'¹⁷ (or 4 years prior if the creditor is a related entity of the company), regardless of the size of the payment and its benefit to other creditors.
- Liquidators would be required to complete and lodge a report to ASIC under Section 533 of the Corporations Act for all companies where there was any suspected wrongdoing (including minor matters that may not indicate intentional misconduct).

As a result of this, insolvency processes will continue to consume the assets of many small businesses in external administration, which can make it harder for the company to restructure if in voluntary administration and decrease the dividend to creditors in liquidation. It remains fairly common for unsecured creditors to get very minimal returns in the liquidation of an incorporated small business.

¹⁵ There is currently no uniform legislative definition of small business. A list of some of the statutory definitions was included in the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry 2018, 'Background Paper 12: Financial services and Small and Medium-Sized Enterprises', p5-6.

¹⁶ Unfair preferences occur where a creditor has received an advantage over other creditors, by receiving payment (or other type of transaction) for their outstanding liabilities and does so in circumstances where they knew, or ought to have known, that the company was insolvent.

¹⁷ The relation back day is the date by which the prescribed period begins whereby transactions entered into by the company may be considered voidable.

The high cost of external administration and the loss of control of the company to the insolvency practitioner in voluntary administration will continue to discourage small businesses from engaging with the system. As a result, the assets of the company may continue to be used up and small businesses that have a chance to go on trading will wind up, with a loss of economic activity and employment and lower returns to creditors. This is of particular concern in the aftermath of COVID-19, where many otherwise viable businesses may have ran up significant debts due to the impact of government-ordered lockdowns and other health measures.

The temporary relief currently allowing insolvency practitioners to more easily communicate with creditors electronically and to hold fully virtual meetings would not be extended. This will require creditors to opt into receiving electronic communication and does not allow for full flexibility in how insolvency practitioners hold meetings.

Option 2 – Introduce simplified insolvency processes for small businesses (based on liabilities below \$1,000,000) and improve the capacity of the insolvency sector

Small business restructuring and liquidation

Option 2 would introduce new insolvency processes targeted at small businesses. These would target the barriers identified above, to ensure they would be accessed, and provide greater benefits to, small businesses.

A new, simplified debt restructuring process would be introduced for eligible small businesses. Unlike voluntary administration, which provides administrators broad powers to support business turnaround, this process would be targeted simply at restructuring a company's debts. In doing so, it is highly targeted at distressed but viable small businesses, who may simply need 'breathing room' to get back on their feet.

The process would require the debtor company to prepare a plan as to how it will restructure in order to maximise returns to creditors while saving the business.

A small business restructuring practitioner (SBRP) would oversee the development and implementation of the plan. The SBRP would be required to certify the plan and its supporting document, then provide the plan and this certification to the company's creditors.

Creditors would vote to accept or reject the plan. There would be no need for a physical meeting, with the voting able to be completed by circulation (including through electronic means). If creditors reject the plan then the company would return to the full control of its directors, who can consider next steps. An accepted plan would be put into effect and overseen by the SBRP.

The process would adopt a debtor-in-possession model, allowing business owners to retain control of their business during restructuring, provided they act within the ordinary course of business. In doing so, it responds to findings raised by the

ASBFEO and others¹⁸, that the appointment of independent administrators is a major disincentive for small businesses in accessing voluntary administration.

To ensure consistency, key aspects of the process would use parameters and definitions from existing law, including voluntary administration and ‘Part IX’ debt agreements in personal insolvency¹⁹. The moratorium on creditor claims provided during restructuring, for example, would be based on that provided during voluntary administration. The process by which a creditor verifies or disputes their claim would take account of rules applying in relation to debt agreements.

Recognising that not all distressed small businesses will succeed in being turned around, this option would introduce a complementary simplified liquidation process. This would recognise the particular circumstances surrounding small business liquidation, in particular the limited asset pool available to fund the administration and to be distributed to creditors.

The simplified liquidation would mean:

- Unfair preference payments would be narrowed for unrelated parties and subject to a materiality threshold. Under the simplified liquidation process, the payments to unrelated parties would not be set aside if they were made over three months from the relation back day, or resulted in the creditor receiving from the company less than \$30,000 in value. The purpose is to prevent the costly pursuit of unfair preference payments, where these are unlikely to relate to misconduct or lead to meaningful returns for the insolvent company’s other creditors.
- There would be no creditor meetings, including ad hoc meetings.
- Abolish ‘committees of inspection’.²⁰
- Reporting to ASIC Section 533 report would only be completed where the liquidator has reasonable grounds to believe that misconduct has occurred, with an additional materiality threshold to prevent reporting in relation to insubstantial compliance.
- Other investigatory and related reporting requirements would be simplified to better reflect the context of a small business liquidation. In particular, the reporting and investigatory requirements associated with the liquidator’s three month report would also be streamlined to focus on the liquidator’s actions to that time, the likely timeframe for ending the liquidation and the likelihood of creditors receiving a dividend.

Safeguards

The small business debt restructuring process would include a number of safeguards, in order to prevent abuse and to maintain important creditor rights:

¹⁸ ASBFEO 2020, Insolvency Practices Inquiry: Final Report

¹⁹ A debt agreement is a formal alternative to personal bankruptcy, where a debtor’s creditors agree to accept part payment of debts owed in equal proportions. A debt agreement is made under Part IX of the *Bankruptcy Act 1966*.

²⁰ A committee appointed from among creditors to advise and supervise the liquidator.

- The role of the SBRP, who would administer the process, remains independent. The practitioner will have important obligations they must fulfil on behalf of creditors (such as certifying the plan and providing this to creditors). The practitioner can also end the process during restructuring, in the event misconduct is identified.
- Businesses would be unable to act outside of the ‘ordinary course of business’ (for example, by selling property) during the process, without the approval of the SBRP.
- Key creditor rights would be preserved. For example, there would be no changes to the rights of secured creditors, and similar types of debts are treated consistently.
- Directors would be required to declare that the company has not engaged in wrongdoing as part of the processes.
- Creditors would retain the right to vote on the debtor company’s proposed plan and the plan must achieve the requisite majority to be binding.

The simplified liquidation process would also include additional safeguards, including the ability of the liquidator to convert the process to full liquidation where they think this appropriate. The same liquidator could then continue with the full liquidation.

Both processes would only be used once by the same directors or companies within a prescribed period (7 years). There would be an exception for companies who have been unsuccessful in developing a restructuring plan, and then seek to enter simplified liquidation shortly afterwards.

Eligibility

Under Option 2, the new processes would be available to businesses with liabilities below \$1,000,000.

Around 76 per cent of companies entering into external administration in 2018-19 had less than \$1 million in liabilities. Of these, around 98 per cent are estimated to be businesses with less than 20 full-time equivalent employees.

Under Option 2, the simplified processes will apply to eligible businesses registered under section 601BA of the Corporations Act. It would not apply to incorporated associations (which are regulated by states and territories) or to unincorporated businesses. Unincorporated business insolvencies are generally governed by the *Bankruptcy Act 1966* rather than the Corporations Act. The *Bankruptcy Act 1966* allows for other forms of restructuring, including Part IX debt agreements.

Increasing the capacity of the insolvency sector

To complement the introduction of new insolvency processes, Option 2 would implement a number of measures to improve the capacity of the insolvency sector.

Increasing the pool of Registered Liquidators

To increase the number of Registered Liquidators to help manage the expected increase in insolvencies Option 2 would include:

- Allowing the Insolvency Practitioner Registration and Disciplinary Committees²¹ (which are the committees that consider the applications of persons to become Registered Liquidators) to register an applicant without conditions even if they do not satisfy all the prescribed statutory criteria, if the Committee believes the applicant to be suitable overall.
- Introducing new categories of eligible employment which can be counted toward the 4,000 hours of relevant employment at senior level that an applicant requires to become a registered liquidator. The new categories would capture: the provisions of advice in relation to the temporary safe harbour (the Government's temporary insolvency relief that relates to insolvent trading and statutory demands) and the permanent safe harbour (the 2017 changes that provides protection for directors from insolvent trading if they take a course of action that is reasonably likely to lead to a better outcome for the company than the immediate appointment of an administrator or liquidator); and, experience in restructuring companies or giving advice in relation to the restructure of companies.
- Allowing the 120 hours of continuing professional education (including the 30 hours required to be objectively verified) to be spread over the three years of the registration period. Currently 40 hours (including the 10 hours required to be objectively verified) must be completed in each of the three years.
- Amending the registration requirements to require only an indirect exposure to or demonstrated knowledge of bankruptcy processes. This is to clarify uncertainty in the law as to whether direct experience with bankruptcy processes at a senior level is required.
- Temporarily waiving fees associated with registration to increase the number of insolvency practitioners in the market. The \$3,500 fee waiver would be in place for around two years so that it could effectively respond to a short-term uptick in insolvencies.

While the provisions mean some registration requirements will be applied in a more flexible way, this is not expected to affect the rigour of the profession. The provisions will be implemented following consultation with industry and there would still remain

²¹ The Insolvency Practitioner Registration and Disciplinary Committees are Committees formed by ASIC on an ad-hoc basis used to register new Registered Liquidators and consider disciplinary matters. Each time a committee is formed by ASIC one committee member will be drawn from a Ministerial pool of appointees. The remaining two members of each committee consist of a representative of ARITA and ASIC.

a requirement that an Insolvency Practitioner Registration and Disciplinary Committee be satisfied that an applicant is suitable to fulfil the functions of a registered liquidator. The additional flexibility provided to the Committees are aimed at ensuring that overly rigid rules that have little benefit in ensuring the integrity of the profession do not prevent suitable persons from becoming a registered liquidator. In addition, the current rigidity may be having negative impacts on the profession. The current continuing professional education requirements, for example, may result in women who have taken maternity leave being no longer eligible to practice, despite their previous experience.

New classification for the SBRP

Option 2 would also create a new classification of insolvency practitioner whose practice would be limited solely to the new simplified restructuring process. Doing so would ensure that the qualifications required of the practitioner working on the new process are in line with the requirements of the role.

The new classification would be a new Registered Liquidator sub-class, as such these practitioners would be assessed by the Insolvency Practitioner Registration and Disciplinary Committees. The Committees would also be responsible for disciplinary action. It would also ensure that capacity constraints around access to the new process can be addressed, as more practitioners will be able to enter the market to meet demand for this work.

The new sub-class is proposed following consultation with a range of stakeholders. Some stakeholders argued that the sub-class should be as broad as possible so as to capture professions with existing relationships among small businesses (such as their regular accountant or financial counsellor). Others opposed the proposition for a new sub-class, arguing that industry does have capacity to manage the expected increase in the number of external administrations or that the new process would benefit from being overseen by a full registered liquidator.

These diverse views were taken into account in setting the requirements for the new sub-class of practitioner. To be eligible for this new sub-class a person must be a fit and proper person and have a public practice certificate (or equivalent) from either CPA Australia, Chartered Accountants Australia and New Zealand (CA ANZ) or the Institute of Public Accountants (IPA). By utilising existing qualifications and membership structures on the part of these professional bodies, the new sub-class will benefit from the use of these bodies' existing processes, including around continuing professional education and disciplinary processes. Importantly, prospective applicants would also need to hold indemnity insurance. In addition, an Insolvency Practitioner Registration and Disciplinary Committee must consider that the applicant is suitable to fulfil the role of a practitioner for the purposes of the new restructuring process.

The criteria for this new subclass of Registered Liquidator has been informed following extensive consultation from a variety of stakeholders. Treasury had bilateral meetings with stakeholders including ARITA, TMA, Law Council, accounting bodies and ASBFEO to discuss the appropriate eligibility requirements. In submissions to the Government's consultations on the exposure draft legislation stakeholders submitted their suggestions for the eligibility requirements.

Temporary relief for company's accessing the new restructuring process

Furthermore, it is anticipated there will be an increase in the number of companies facing insolvency following expiry of the temporary measures due to the impact of COVID-19. For example, as explained above, it can be extrapolated from ASIC data that by the end of the year around 3,000 companies that would have normally gone into external administration will not have. It will be important to manage any potential 'wave' when it is most acute, so that companies who need to access insolvency services can do so. This is particularly important where these involve restructuring, and the possible saving of the company.

As such, a mechanism is proposed to stagger the companies anticipated to access the simplified restructuring process when it becomes available. This would reduce the spike in demand that would otherwise occur when temporary support is withdrawn, and provide industry sufficient time to adapt to administering the new framework. It would use existing and known mechanisms (in the form of the current temporary insolvency relief) to achieve this.

Specifically, how the mechanism would work is that between 1 January and 31 March 2021 a company can announce its intention to access the simplified restructuring process, including by notice through ASIC's published notices website. Once this is announced, the Government's temporary COVID-19 insolvency relief (that relates to insolvent trading liability and to statutory demands) would apply to the company. The company would then have 3 months (from announcement) to consult an SBRP around access to the simplified process. These settings would functionally extend the relief already provided as part of the Government's temporary insolvency measures, where a distressed company must wait to engage an SBRP. As such, the settings would be familiar to both debtor companies and their creditors, helping them to understand the mechanism.

Technology neutrality in insolvency processes

Finally, Option 2 would also help to manage the upcoming wave of insolvencies by modifying insolvency law so that they are technology neutral. It would amend the external administration provisions of the Corporations Act to better enable technologically neutral practices during insolvency processes, namely by making it easier to communicate electronically and by permitting fully virtual meetings of creditors.

Option 3 – Introduce simplified insolvency processes for small (based on small businesses being eligible under a current legislative definitions of small businesses) and improve the capacity of the insolvency sector

Option 3 involves introducing the same new processes as in Option 2 but rather than having an eligibility threshold based on the company's liabilities, the threshold would be based on an existing small business definition in Government legislation.

Treasury has identified over 30 discrete definitions of small business across Commonwealth legislation and instruments. Some definitions are based on the number of employees. For example, the *Fair Work Act 2009* defines a 'small business employer' as an employer that employs fewer than 15 employees at the relevant time

while the *Financial Services Reform (Consequential Provisions) Act 2001* uses fewer than 20 employees unless it is a manufacturing business where a small business is defined as having fewer than 100 employees. Instead of number of employees some legislation uses a definition of aggregate turnover. For example, the *Income Tax Assessment Act 1997* includes different turnover thresholds for different small business concessions.

4. What is the likely net benefit for each option?

Option 1 – Status Quo

If no reforms are progressed and the status quo persists, then small businesses and their creditors and employees will continue to be negatively impacted through reduced returns as the limited assets of small businesses are consumed by the cost of the external administration process, or the businesses are discouraged from using the system.

Under Option 1 the insolvency framework would not fully accommodate the needs of Australian small businesses. These include:

- The need to ensure that regulatory obligations are commensurate with the complexity of the business and the likelihood of misconduct.
- The need to maximise the opportunity for distressed but viable companies to restructure and survive.
- The need to maximise returns for creditors in the event that a business is wound up.

Australian businesses would continue to only be able to access insolvency processes that are the same no matter the size of the business; processes that are better suited to larger, more complex company failures, which may have greater means to engage in sophisticated forms of misconduct.

That said, reforms to address the current inefficiencies may introduce new complexity and would require industry and the insolvency sector to become familiar with any changes. This poses challenges, given that there will likely be a rise in the number of companies entering external administration following the withdrawal of temporary insolvency measures at the end of 2020. Thus, the main benefit of Option 1 is it ensures parties affected by the insolvency system remain familiar with how the system works by not making changes to it.

While maintaining the status quo may provide more certainty, it may also result in some viable companies going out of business or viable companies not being able to access professional support. Small business owners would be required to engage with current processes that have been described by stakeholders that represent both the insolvency industry (ARITA) and the small business sector (ASBFEO) as failing small businesses.

Furthermore, under Option 1 requirements to provide notice documents in hard copy by post, and to hold meetings in physical locations (even if participants would prefer

to attend virtually) would remain. These unnecessarily requirements can consume assets possibly lowering the returns to creditors.

There is no impact to the Government's underlying cash balance with this option.

Option 2 – Introduce simplified insolvency processes (liabilities below \$1,000,000) and improve the capacity of the insolvency sector (preferred option)

This option would apply the simplified framework to companies with liabilities of up to \$1 million. This would cover around 76 per cent of external administrations of which around 98 per cent are estimated to involve companies with less than 20 FTE employees (based on companies entering external administration in 2018-19, for context in 2018-19 there were 8,105 companies that entered external administration). This would deliver substantial regulatory savings and would deliver action in an area stakeholder feedback has consistently identified as high priority. Businesses that are insolvent that can't rely on the safe harbour for protection from insolvent trading have no choice but to access an external administration process. Without the option of simplified restructuring they may be forced into a costly full liquidation.

Small business restructuring and liquidation

The simplified restructuring process would enable a debtor-in-possession model, whereby the directors of the company would remain in control throughout the process. Further, only directors could put forward a reorganisation plan. This differs from the current model used in voluntary administration, where the administrator takes full control of the company and is responsible for trying to work out a way to save either the company or its business.

The benefits of a debtor-in-possession model is that it provides business owners with more control over the process will mean the process is more aligned the needs and preferences of business owners, who will then be more amenable to its use. This will encourage them to engage in restructure when their business may still be viable, increasing the chances of its survival. The ASBFEO in their *Insolvency Inquiry Report* described how the current external administration processes is not working for small businesses:

Small business owners report facing an opaque system, where decisions are taken out of their hands, they feel pushed into outcomes they were not looking for, and their expertise or knowledge of the business they have been running is discounted or ignored.

On the other hand, some may argue that it may not be appropriate for the small business owner to remain in control of the business particularly if they may have contributed to the business failure through misconduct. Thus transferring control to an administrator may allow for more business to restructure, be transferred to new management, and enhance the ability to identify misconduct. However, this reasoning is not consistent with the evidence stated above and the ability to design a debtor in possession model that appropriately balances and manages risks associated with misconduct.

The simplified liquidation pathway for small businesses will allow faster and lower-cost liquidation, increasing returns for creditors and employees. Under the new process, regulatory obligations will be simplified, so that they are commensurate to the asset base, complexity and risk profile of eligible small businesses. In practice simplified liquidation will reduce investigative requirements, requirements to call meetings and reduce reporting function. This will free up value for creditors and employees, and allow assets to be quickly reallocated elsewhere in the economy, supporting productivity and growth. While a simplified liquidation process aims to increase the returns to creditors this may not be possible in all cases. It is expected a number of simplified liquidations will still result in no returns being distributed to some creditors but even in such cases there will be benefits in terms of lower cost, better access to liquidation services, and a quicker liquidation.

A similar proposal to the simplified liquidation process was previously recommended by the Productivity Commission in its 2015 inquiry into [Business Set-Up, Transfer and Closure](#). The Productivity Commission's simplified liquidation however, had an eligibility threshold of \$250,000 of liabilities to unrelated parties (this was the same threshold recommended by ARITA in their proposed streamlined liquidation).

In the case of this option, the \$1 million eligibility threshold was chosen because it allowed for simplicity and broad coverage, while being a good indicator of the complexity of an insolvency. During consultation on this option, the Government heard a broad range of views from stakeholders on the appropriateness of the threshold, including that the \$1 million threshold was both too low and too high. This is outlined in more detail at section 5. Upon considering these views, it was decided the \$1 million threshold was appropriate.

The benefits of simplified restructuring and liquidation results in regulatory savings for businesses and individuals. Estimated total regulatory savings flowing from the new restructuring process are estimated to be \$23 million per year (based on an average over 10 years). Estimated total regulatory savings for changes to liquidation are estimated to be \$105 million per year (based on an average over 10 years).

COVID-19 has exacerbated the impacts of shortfalls with our current system, on creditors, business and the economy. To maximise the benefits of these reforms ideally they should be in place before the expected increase in companies going through external administration occurs following the winding back of temporary support measures. Option 2 also addresses concerns that industry and companies will not be ready for the 1 January 2021 start date. In particular, Option 2 proposes that between 1 January and 31 March 2021, a company can announce its intention to access the simplified restructuring process. Once this is announced, the existing temporary insolvency relief would apply to the company. This helps mitigate the potential risks in making substantial changes during the crisis.

Methodology

This option assumes a baseline of around 4,400 businesses accessing the simplified liquidation process a year. This is based on the assumption that all eligible businesses (businesses with liabilities under \$1,000,000) access the simplified process, with the estimated number of eligible businesses based on ASIC data from 2018-19 on

external administration. An increase in the number of insolvencies is assumed for the first few years due to the impacts of COVID-19.

For each simplified process, the overall administrative savings (from reduced time spent on meetings, investigations and reporting) would equal around five days. This is based on reduced days the insolvency practitioner spends on investigative functions, preparing and attending meetings and time spent reporting. The regulatory costs imposed on the insolvency practitioners may ultimately be borne by the creditors as the greater the costs of the administration the smaller the ultimate returns to creditors. These creditors can be businesses or individuals. Treasury has estimated that 70 per cent of the creditors are businesses with the rest being individuals. Based on ASIC data an external administration has on average of 20 creditors. To calculate the hourly regulatory burden the standard OBPR rates of \$73.05 for businesses and \$32 for individuals have been used. Individuals reflects employees seeking owe income (who are typically the single largest group of creditors), as well as customers who have missed out on goods and services purchased in advance. Based on the average cost of remunerating an insolvency practitioner and running processes like meetings, this would produce estimated savings of (on average over 10 years) around \$105 million annually, with \$75 million annually going to businesses and \$30 million annually going to individuals.

For restructuring, we assume that around 850 businesses will access the process every year (informed by the number that currently use voluntary administration procedures, which is significantly less than the number which currently enter liquidation). This assumes a time saving of around 2.5 days versus voluntary administration (associated with less time spent on debt processes and investigative function). The same base assumptions as mentioned in the simplified restructuring also apply for the simplified reorganisation process. This would produce estimated total regulatory savings of (on average over 10 years) around \$23 million annually, with \$17 million annually going to businesses and \$6 million annually going to individuals.

While there would be a reduction over time in the number of companies which can utilise the simplified processes, due to the safeguard which means each process can only be used once by the same company/directors every 7 years, this has not been factored into the estimated take-up as we anticipate this to be a negligible number of companies compared to the increase in the number of companies which fail/are financially distressed each year. Also, this number would be offset by companies that are able to access the new simplified process but would not be able to access voluntary administration due to the costs associated with that process.

We have not factored in impacts that the new processes may have in abating unlawful company abandonment (where directors simply leave companies, rather than having them wound up by an insolvency practitioner). As this conduct is unlawful it is not clear whether reduced regulatory burden on company directors and greater returns for creditors will have a meaningful impact on it.

Increasing the capacity of the insolvency sector

In 2018-19, there were 648 Registered Liquidators in Australia, fewer than there were 10 years ago. Currently, it costs around \$3,500 to apply and register to become a Registered Liquidator. Temporarily removing this cost would encourage and enable

more suitable practitioners to enter (or re-enter) the market. Allowing for more flexibility in the registration of insolvency practitioners and temporarily waiving fees associated with registration as a Registered Liquidator will help to increase the number of Registered Liquidators which will help to manage the expected increase in insolvencies. As well as increasing the number of Registered Liquidators, the new classification of insolvency practitioners whose practice will be limited solely to the new simplified restructuring process will help support the capacity of the system. The new sub-class of Registered Liquidator may have an impact on some already established Registered Liquidators as they may lose some business due to the increased competition in the market. Furthermore, allowing companies to announce their intention to access the simplified restructuring process will help manage an anticipated increase in the number of companies entering external administration. However, becoming a Registered Liquidator and announcing your intention to restructure are optional so these changes are unlikely to have a material impact on regulatory savings.

There may be a risk that given the new conditions the Insolvency Practitioner Registration and Disciplinary Committees may register unsuitable people to become Registered Liquidators. However, this is unlikely given the membership and composition of Committees, and the benefits from giving Committees greater flexibility to perform their role outweighs the risk. Many requirements, such as the applicant being a 'fit and proper person' remain. The new flexibility allows the Committees to better use their expertise and perform their duties.

Option 2 would also help to manage the upcoming wave of insolvencies by modifying insolvency law so that it is more technologically neutral. It would amend the external administration provisions of the Corporations Act to enable technology neutral practices during insolvency processes, namely by:

- Removing the requirement for creditors to have to opt into receiving electronic communication, thereby allowing insolvency practitioners to send communications electronically if an electronic address is available.
- Giving insolvency practitioners the option to conduct meetings entirely virtually. Under the current legislation meetings are required to have a physical location and alternate locations can be linked in virtually.

Doing so will ensure that insolvency processes can be carried out as efficiently and as cost effectively as possible, while still maintaining creditors' rights related to notification, participation and attendance. This will ensure that administrators can focus on the substantive requirements of their role, meaning they will be better placed to deal with an increase in demand for their services. Applying the changes to existing and new insolvency processes will ensure broad coverage, while building on the simplicity and cost savings that the new processes will deliver. The regulatory savings for allowing electronic communications and for moving to online meetings are estimated to be around \$36 million per year (on average over 10 years).

Methodology

This option assumes a baseline of around 8,100 businesses entering external administration, based on ASIC data from 2018-19. All companies in external administration can utilise the changes to make the external administration technology neutral not just small businesses. Treasury estimates that 40 per cent of external administrations would be held completely virtually and on average an external administration has 2 to 3 meetings.²²

Time cost of printing and other mailroom activities involved in sending a letter is assumed to be six minutes. While sending an electronic document takes one minute. The regulatory saving time is calculated using the OBPR work-related labour cost of \$73.05 per hour. Printing and postal costs per actual letter are respectively \$1.50 and \$2.20.

As with the small business processes the average number of creditors is assumed to be 20 and an increase in the number of insolvencies is assumed for the first few years due to the impacts of COVID-19.

Based on these assumptions the regulatory savings for allowing electronic communications are estimated to be around \$3 million per year (on average over 10 years) with the regulatory savings for allowing fully virtual creditor meetings to be around \$33 million per year (on average over 10 years).

These regulatory savings should allow for greater returns for creditors when a company is liquidated or restructured. The reforms should also help insolvency practitioners manage capacity in the system with the expected increase in work-load from the anticipated rise in insolvencies relating to COVID-19, as well as enabling more small businesses to successfully restructure.

In total the estimated savings for Option 2 (on average over 10 years) is around \$165 million annually, with \$129 million annually going to businesses and \$36 million annually going to individuals.

With regard to the cost to Government, there is a very minor estimated positive impact on underlying cash balance of approximately \$0.4 million. This is the net result of a small increase in application fees from registered liquidators across each year of the forward estimates (due to an increase in liquidators being registered) minus the lost revenue from the waiver of registration fees for liquidators entering or re-entering the market in 2020-21 and 2021-22.

Average annual regulatory costs (from business as usual)				
Change in costs (\$ million)	Business	Community organisations	Individuals	Total change in cost

²² During the period after which the temporary insolvency relief was implemented, Treasury held consultations, including with stakeholders from industry, to understand the dynamic of virtual meetings, and how these were being utilised and received by participants. This information has informed these assumptions.

Average annual regulatory costs (from business as usual)

Total, by sector	-\$129	\$0	-\$36	-\$165
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Option 3 – Introduce simplified insolvency processes (based on small businesses being eligible under a current legislative definitions of small businesses) and improve the capacity of the insolvency sector

Option 3 uses an alternative threshold for determining which small businesses are eligible but is otherwise the same. An alternative threshold based on a business having less than 20 FTE employees would have captured around 5,500 businesses in liquidation and 1,100 businesses in voluntary administration in 2018-19.

For the purpose of calculations this option uses the definition of having less than 20 full-time equivalent (FTE) employees as it matches available ASIC data.

Capturing a higher number of businesses than in Option 2 results in Option 3 having a higher regulatory saving. Estimated regulatory savings for changes to liquidation are estimated to be \$126 million per year (based on an average over 10 years) and for restructuring are estimated to be \$29 million per year (based on an average over 10 years). As in Option 2 the regulatory savings for allowing electronic communications are estimated to be around \$3 million per year (on average over 10 years) and the regulatory savings for moving to online meetings to be around \$33 million per year (on average over 10 years). This equates to total estimated savings of around \$192 million annually (on average over 10 years), with \$152 million annually going to businesses and \$40 million annually going to individuals.

Although regulatory savings may be higher, the number of employees is not considered the most appropriate way to determine eligibility. It is harder to appropriately target these changes to suitable businesses with a threshold based on employees. For example, a large complex business with large liabilities but with a mainly automated process and consequently a low number of employees may qualify under an employee based test. Data from ASIC shows that in 2018-19 there were over 100 companies which entered external administration with over \$10 million in liabilities but with less than 5 FTE employees. It poses integrity risks for a debt of this scale to be captured under a simplified process. Having companies with relatively high liabilities (in some cases over \$10 million) accessing a process that is designed to be simplified could have a negative impact on creditors. Unlike Option 2, under Option 3 the new simplified processes may not be commensurate to the asset base, complexity and risk profile of eligible small businesses.

There are also problems with the opposite situation. A simple business, with low debt levels but with over 20 FTE employees would miss out on the streamlined process, even when it may be appropriate for them to be included. Data from ASIC shows that in 2018-19 there were over 100 companies which entered external administration with under \$1 million in liabilities but with 20 or more FTE employees. In these cases creditors and other affected parties may miss out on better outcomes that may be available to them had the company been able to go through a streamlined process.

Furthermore, the number of employees may not be an accurate indicator for companies near end of life where they may have made staff redundant. In comparison the amount of liabilities is relatively easier to understand and calculate, reflects the indebtedness of the company and creditor exposure to loss, and is difficult to manipulate. In addition, the Productivity Commission and others advocating for small business liquidation have recommended a liabilities test. In consultation the majority of stakeholders preferred a liability threshold over other types of thresholds. Similar arguments can be made for using existing definitions that use aggregate turnover instead of employees. A financially distressed business's turnover may not be reflective of its size (it is likely to be lower than would otherwise be case) or creditor exposure to the failure, and may be difficult to measure or verify.

With regard to the cost to Government, there is a very minor estimated positive impact on underlying cash balance of approximately \$0.4 million. This is the net result of a small increase in application fees from registered liquidators across each year of the forward estimates (due to an increase in liquidators being registered) minus the lost revenue from the waiver of registration fees for liquidators entering or re-entering the market in 2020-21 and 2021-22.

Average annual regulatory costs (from business as usual)				
Change in costs (\$ million)	Business	Community organisations	Individuals	Total change in cost
Total, by sector	-\$152	\$0	-\$40	-\$192

5. Who did you consult and how did you incorporate their feedback?

Consultation prior to announcement

On 24 September 2020, the Treasurer announced the broad framework for the insolvency reforms to support small business.

Prior to the announcement, Treasury held regular consultation with key stakeholders following the implementation of the temporary insolvency relief from March 2020. Consultation was held with various stakeholders groups including representatives of insolvency practitioners, turnaround professionals, accountants and other professionals, and small business representatives.

While the purpose of this consultation was to gauge the impact of the insolvency relief and to better understand the state of the market, stakeholders raised broader issues during these meetings. These included broader, systemic issues with Australia's insolvency framework, and the impact of these issues on business (including small businesses) in the context of COVID-19.

Issues raised included:

- The impact of extensive obligations during insolvency processing on both practitioners and business.
- How Australia’s insolvency system could deal with problem of highly indebted small businesses in the aftermath of COVID-19.
- Capacity in the insolvency sector.

Feedback from these meetings was used to inform our understanding of the insolvency system, the problems facing the system, options for reform, and approaches to implement those options.

Impact of stakeholder reports and proposals

As well as conducting stakeholder meetings, Treasury analysed existing submissions and reports and used these to inform the reform proposal. These included:

- The Productivity Commission’s 2015 inquiry *Business Set-up, Transfer and Closure*, proposed that the Government adopt a streamlined liquidation process for small businesses, stating, “... there is considerable scope to streamline insolvency processes for the majority of businesses through the creation of a two stream approach.”²³
- ARITA, in its 2015 submission to the Productivity Commission review above, released a discussion paper proposing both a streamlined insolvency process and a new debt restructuring process for micro businesses.²⁴ ARITA reiterated its proposal in its submission to ASBFEO’s insolvency practices inquiry in January 2020.²⁵
- The ASBFEO, in its 2020 insolvency practices inquiry, also recommended the Government adopt streamlined insolvency processes for small businesses and argued the current regime was not working for small businesses.²⁶

These proposals, as well as broader feedback on Australia’s insolvency framework, were closely considered in the development of the reforms. We also note that both the Productivity Commission and the ASBFEO consulted with a range of stakeholders in undertaking their respective inquiries, meaning their reports reflect the views of a broader group of stakeholders.

Bilateral consultation following the announcement

Following the Government’s announcement of the reforms, Treasury met with a variety of stakeholders including ARITA, TMA, ASBFEO, Law Council of Australia,

²³ Productivity Commission 2015, *Business Set-up, Transfer and Closure*: Productivity Commission Inquiry Report, p. 28.

²⁴ ARITA 2015, *Submission to Productivity Commission review on Business Set-up, Transfer and Closure*.

²⁵ ARITA 2020, *Submission to the Insolvency Practices Inquiry*, p. 23, https://www.arita.com.au/ARITA/News/Submissions/Australian_Small_Business_and_Family_Enterprise_Ombudsman_s_Insolvency_Practices_Inquiry.aspx

²⁶ ASBFEO 2020, *Insolvency Practices Inquiry: Final Report*.

Chartered Accountants Australia & New Zealand (CA ANZ), KPMG, the ABA, the Council of Small Business Organisations Australia (COSBOA) and the Property Council. The purpose of the consultation was to allow stakeholders to communicate their high-level views on the reform process, and to ask questions, before the draft legislation was finalised.

Generally, stakeholders voiced strong support for both the design and objectives of the new simplified insolvency processes for small businesses. Concerns, where these did exist, centred on aspects of the restructuring process, including the rights for creditors, the coverage of the moratorium on creditor claims during the restructuring process, and the potential for debtor companies to take advantage of the process. It was proposed that the coverage of the moratorium and the approach to secured creditor rights would closely reflect those provided during voluntary administration. This approach was endorsed by most stakeholders, and was subsequently reflected in legislation. Stakeholders were also generally supportive of proposed provisions preventing misuse of the process including limitations on its reuse and the need for directors to declare that they had not engaged in creditor defeating conduct.

Consultation on the draft legislation

To maximise flexibility and opportunities for stakeholder feedback, the primary legislation aimed to establish the broad framework, while allowing for key design aspects to be progressed in subordinate legislation (rules and regulations). This included the eligibility criteria to access the new processes, the qualifications for the SBRP, and the more detailed mechanics for the new restructuring process. This approach allowed for two separate periods of public consultation. A shorter time for formal consultation received approval from the Legislative and Governance Forum on Corporations (LGFC).

On 4 October 2020 the exposure draft insolvency reforms Bill was made available to a number of stakeholders with whom Treasury had already consulted on the policy and on 7 October 2020²⁷ it was made publicly available on the Treasury website with consultation closing on 12 October 2020. The shortened consultation periods intended to allow for the legislation to be passed and the reforms to commence on 1 January 2020 in line with the expiry of the temporary insolvency relief on 31 December 2020.

The Government received 51 submissions in response to the exposure draft of the primary law amendments, showing strong stakeholder interest and engagement. A log of the submissions is at Annex 1. The vast majority of submissions were supportive of the objectives and the broad parameters of the reform proposal. Stakeholders submitted some policy considerations as well as suggestions on the technical drafting of the legislation.

The major policy issues raised related to the qualification requirements for the new SBRP, the threshold for eligibility to access the new simplified insolvency processes, and suggestions on how the primary law could best implement the announced reforms.

²⁷ Due to the proximity to the release of Budget 2020-21 the exposure draft legislation could not be released until 7 October 2020.

Consultation on the draft subordinate legislation

Following the finalisation of the Bill, exposure draft regulations and rules were released for public consultation from 17 – 24 November, during which time they were available on the Treasury website. Treasury also provided these documents to a number of stakeholders, and met with several stakeholders to discuss the exposure drafts.

As at 25 November, Treasury had received 20 submissions on the draft subordinate legislation. A log of these submissions is at Annex 2. Bilateral consultation was also held with stakeholders including the Law Council, ARITA and the TMA.

Major policy issues raised in response to the draft regulations and rules included the qualification requirements for the new SBRP, which debts could be included under a plan, the terms of a plan (including how long it could last for), and issues related to how a plan is put to creditors and voted on.

Qualifications to register as an SBRP

The proposed qualification requirements for the SBRP have been informed from feedback received during consultation. This was an issue for stakeholders, who expressed their views in both bilateral consultations and in submissions.

Some stakeholders argued that the sub-class should be broad enough to capture appropriate professions with existing relationships among small businesses (such as their regular accountant or financial counsellor). In its submission on the draft legislation, the TMA stated:

Due to Australia's economic success over generations there is a lack of an SME restructuring profession that is readily identifiable. It needs to be grown. In absence of that and for this reason we believe the best means of expanding the number of qualified persons who are able to perform all steps associated with the small business restructure other than an ordinary or simplified liquidation is to look to the criteria set out below. In short, the best people to help restructure a small business will be local senior accountants and possibly lawyers, particularly in suburban and regional Australia. For businesses in the agricultural sector (including farmers), involvement of rural debt counsellors may also be appropriate.

Others voiced concern around the proposition for a new subcategory. For example, in its submission on the draft legislation, ARITA stated:

We are concerned that a new sub-class of registration for restructuring practitioners with lower qualifications, experience, knowledge or abilities requirements undermines the basis of the 2016 amendments.

This places at risk progress demanded by successive Parliamentary Inquiries into insolvency that demanded higher levels of qualification and skill across all forms of insolvency administration.

Some stakeholders voiced concern that the industry may have capacity to manage the expected increase in the number of external administrations, meaning there is no need to expand the requirement from the current requirements to be a Registered Liquidator. For example, in its submission on the draft legislation, the Business Law Section of the Law Council of Australia (Law Council) stated:

We recommend that before any decision is made to permit some lesser qualified category of practitioner to undertake such a role, some time is taken to see if the current insolvency market is able to provide adequate numbers of suitably qualified registered liquidators to cope with immediate demand that is anticipated after the proposed commencement date of 1 January 2021. Any additional time that current practitioners may need to cope with the immediate demand could be provided by granting, in the regulations, a temporary extension to the proposed restructure periods (say, for the first three months of 2021).

The proposed requirements for registration as an SBRP reflect a balance between these views. As noted, it is proposed that, to be eligible to register as an SBRP, a person must be a fit and proper person, have a public practice certificate from either CPA Australia, Chartered Accountants Australia and New Zealand (CA ANZ) or the Institute of Public Accountants (IPA) and be assessed by a registration committee as suitable. This widens the pool of professionals who can perform these services, a key priority of many stakeholders. At the same time, it addresses stakeholder concerns around preventing unscrupulous or unqualified advisers from being appointed as an SBRP.

Eligibility to access the new simplified insolvency processes

In submissions received on the draft legislation, the Government received a range of feedback on the threshold for eligibility to use the new insolvency processes:

- The majority of stakeholders preferred a liability threshold of some variety.
- Some stakeholders requested the liability threshold be coupled with another definition of small business to make sure it was properly targeted.
- Others suggested eligibility should be linked with already existing small business definitions.

Stakeholders also had divergent views on the amount that the liability thresholds should be set at. Some stakeholders believed that a \$1 million threshold was too high. They argued that a \$1 million threshold would capture some larger businesses that would not be suited to the processes, and potentially increase the risk of illegal phoenixing. For example, ARITA, in the covering letter to its submission on the draft legislation, stated:

We hold significant concerns with the foreshadowed eligibility liability threshold for both the proposed restructuring and simplified liquidation processes of \$1 million. We believe that a liability threshold of \$250,000 of unrelated debts is more appropriate and more reflective of the small, non-complex businesses the reforms are aimed at. We believe that a \$1 million

threshold is too high, capturing a significant proportion of external administrations and enhancing the risk of this framework being used for phoenixing.

However, other stakeholders had a different perspective, requesting consideration be given to increasing the \$1 million threshold. The intent behind this view was that a higher threshold would allow more businesses to benefit from the new processes. For example, the TMA, in its submission on the draft legislation, stated:

We note that a cap based on a maximum of \$1 million in liabilities would appear to be lower than the caps applicable to small business restructuring processes or small business liquidation proceedings in other jurisdictions...

Consideration should therefore be given to whether a higher threshold would be appropriate either now or at some point in the future to ensure that the restructuring process has utility beyond very small companies.

In addition, some stakeholders also argued the threshold should be different for simplified liquidation as compared to the proposed restructuring process.

On balance after considering the feedback received, a \$1 million threshold is considered appropriate. This is because:

- A liabilities threshold is the simplest and most effective conduit for the complexity of an insolvency, a fact some stakeholders acknowledged. It appropriately focuses on creditor exposure and is relatively transparent, easily measured and difficult to manipulate. For this reason, a liabilities threshold was previously proposed by both ARITA and the Productivity Commission (albeit at a lower value). A liabilities test is used elsewhere to determine access to small business insolvency processes, including under Chapter 11 of the United States Bankruptcy Code.
- Alternative thresholds linked to existing small business definitions (for example, those based on FTE employees) introduce their own complexity (for example, in requiring companies to calculate how many part-time staff constitute a fixed number of FTE employees). These alternate approaches may be easier to mismeasure or manipulate, and may not accurately represent the complexity of an actual insolvency. Consistency benefits would also be lost if a definition linked to another law was changed.
- Setting the threshold at \$1 million will pick up an appropriate proportion of companies who enter insolvency processes (estimated at around 76 per cent, based on historical insolvency statistics). This responds to a key stakeholder concern, which was to ensure the process is available to as large a number of companies as possible. While the \$1 million threshold is higher than that previously proposed by ARITA and the Productivity Commission, some stakeholders argued it should be higher while others supported it. As noted, additional protections already exist to guard against illegal phoenixing.

The provisions setting out eligibility for the process are set out in the regulations.

Length of a restructuring plan

The draft regulations proposed that a restructuring plan could run for a period of up to five years. There were mixed views on whether this was an appropriate timeframe.

The policy intent of the five year period was to provide debtor companies sufficient flexibility to pay off debts under the plan. However, some stakeholders proposed a shorter maximum period, noting that a shorter period would reduce uncertainty around whether creditors would be paid, thereby providing more confidence. Stakeholders also noted that timeframes for repayment under similar regimes, including deeds of company arrangements and Part IX debt agreements, are typically shorter than what was being proposed.

For example, in its submission on the exposure draft regulations and rules, the Australian Banking Association stated:

Under regulation 5.3B.13(4)(b) a restructuring plan may provide for payments to be made for a period of up to 5 years. Given the aim of the restructuring process is to effect an expedited restructuring of small business this period is too long. The expectation is that small businesses utilising the restructuring process will have relatively simple debt structures and simple assets to be realised to satisfy those debts. Such assets should be capable of being realised within a short period of time. The restructuring period should reflect the aim of quickly restructuring small business.

Under existing comparable regimes – voluntary administration and deeds of company arrangement -timeframes for repayment are usually much shorter than 5 years. The restructuring plan should allow for payments over a period of no more than 1 to 2 years. The longer a restructuring plan is in place, the longer uncertainty about the business's financial capacity will remain, restrict its access to capital and allows for costs to be incurred. The proposed period of up to 5 years does not appear consistent with the aims of the new process.

In light of this feedback, the maximum period for a restructuring plan was amended to 3 years. This was designed to balance the concerns raised by some stakeholders with the original policy intent of providing appropriate flexibility for the debtor company. This also reflects the period for which a Part IX debt agreement can run (in instances where the debtor does not own their home).

Amendments to the maximum period for a plan were made in the final regulations.

Admitting new debts to a plan

The exposure draft proposed that creditors would have 5 business days in which they could request to vary their claims following the provision of a plan to the creditor. This timeframe was put in place so that the practitioner would have sufficient time to respond to this request for variation. It was also proposed that only unrelated creditors (who were not in an existing plan) could request to enter a plan once it was made. The intent was to minimise the risk of related parties not fully disclosing debts up front in order to promote a company's access to the new process.

During consultation on the regulations, stakeholders expressed several concerns around this process:

- Some stakeholders raised concern that the 5 business day period in which creditors had to certify or request to vary their claim was too short.
- Some stakeholders raised concerns about the circumstances in which new creditors could be admitted to the plan.
- Some stakeholders raised concerns that existing creditors lacked an avenue to amend their claim, if extraordinary circumstances prevented it from being made in the first instance.

The final design of the law sought to balance these various interests and concerns. In particular, the draft law was amended so that:

- Creditors would have 5 business days in which they could request to vary their claims following the provision of a plan to creditors.
- The SBRP could choose to consider variations after this period, and up to the making of a plan, provided the creditor provides a justification as to why this wasn't provided in the initial five business day period.
- Following the making of a plan, new creditors as well as variation requests from existing creditors can be admitted into the plan, where the creditor provides a justification as to why this request wasn't provided prior to the making of the plan. The SBRP then has discretion to admit these requests in appropriate circumstances.

This approach seeks to address stakeholder concerns and to ensure policy objectives are met, by:

- Ensuring there is an incentive for creditors to lodge any requests to vary their claims in the initial five day period.
- Providing a means by which requests for variation can be admitted after this period, but at the discretion of the SBRP.
- Providing a means to admit variations and new claims after the plan is made, but using a suitably high threshold (thereby providing certainty for existing creditors who have endorsed and are party to the plan).

Remuneration for SBRPs

The exposure draft Rules specified that remuneration for an SBRP could only take the form of amount specified prior to their appointment, and agreed with by the board of the company that had appointed them. The intent of this 'fixed' fee was to ensure transparency around the price of an SBRP's services, and to encourage competition in the market for these services.

Several stakeholders raised concerns about the impact of a fixed fee structure, particularly in the event that the SBRP faced costs that were not anticipated when the

cost was settled. A major concern included the costs that an SBRP could face as a result of litigation.

For example, in its covering letter on its submission on the exposure draft regulations and rules, ARITA stated:

The level of uncertainty and possible complexity, including the potential for litigation, for a set fee is likely to dissuade many experienced practitioners from accepting an appointment as a restructuring practitioner.

To address this concern, the final Rules include an exemption from the fixed fee structure for costs incurred by an SBRP, where these are associated with defending legal actions brought by other parties. The intent is to remove the potential for a major, and uncertain, variant on the expected cost of a restructuring. The exemption only extends to defending legal actions, so there is no incentive for the SBRP to launch legal action themselves. At the same time, the broad benefits of the fixed structure are retained.

Technical and operational changes

In response to stakeholder feedback and further review, further amendments were made to the primary legislation in the period following consultation on the draft Bill. These are largely based on issues that stakeholders raised and which they argued were important to ensure the effective operation of the new processes. Examples of the changes include:

- amending the ipso facto stay provisions (which prevent creditors from terminating contracts because of an insolvency event) applying during the debt restructuring process so that they apply to contracts entered into from 1 July 2018. This aligns with the scope of the ipso facto stays currently provided for companies in voluntary administration.
- clarifying that debts incurred during the debt restructuring process prior to making a restructuring plan will be provable (that is, claimable by a creditor) in the event that the company subsequently enters liquidation.
- providing a new regulation making power, which allows for regulations to specify cases that are or are not in the ‘ordinary course of business’. Under the new restructuring process, company directors must seek approval from a small business restructuring practitioner for actions that fall outside this threshold.

During consultations, stakeholders indicated support for these changes which are reflected in the primary legislation.

In response to stakeholder feedback, further amendments were also made to the regulations and rules to ensure they operated as intended. These included:

- ensuring that the provisions around more flexible continuing professional education (CPE) requirements for registered liquidators operated effectively

(that is, that they benefited existing registered liquidators, not just those who had newly registered);

- ensuring that the requirements around notification of creditors are applied consistently (for example, that creditors are notified where a plan lapses, regardless of the reason for it lapsing); and
- addressing instances where there were inconsistencies in terminology between the draft regulations and the Bill.

6. What is the best option from those you have considered?

Option 2 is the preferred Option as it produces a number of regulatory savings and other improvements to the insolvency regime, while being appropriately targeted and addressing the risk of misconduct. The benefits for Option 2 include:

- Lowers the costs of liquidation and restructuring for small businesses, promoting higher returns for creditors when insolvent businesses are required by law to enter an insolvency process.
- Removes processes which are not necessary for small businesses.
- Allows more businesses to successfully restructure when they face insolvency, rather than having to access an alternative process like liquidation.
- Provides more control to business owners and encourages them to restructure.
- Keeps important safeguards to protect against corporate misconduct including illegal phoenix activity.
- Requires more complex businesses to go through the full liquidation and voluntary administration processes.
- Helps to manage any anticipated wave of external administration.
- Increases industry capacity to deal with an increased number of external administrations effectively and efficiently, so that the market can better respond to changes in demand for insolvency services including in the aftermath of COVID-19.
- Changes registration requirements for insolvency practitioners to improve industry capacity and diversity.
- Reduces fees to encourage new practitioners, boosting capacity and competition.
- Enables greater usage of technology neutral practices in insolvency processes.

7. How will you implement and evaluate your chosen option?

The chosen option will be implemented through legislative changes to the *Corporations Act 2001* and related subordinate legislation. Subordinate legislation includes changes to the *Corporations Amendment (Corporate Insolvency Reforms) Regulations 2020*, *ASIC Supervisory Cost Recovery Levy Regulations 2017* and the *Corporations (Fees) Regulations 2001*, as well as rules made under the *Corporations Act 2001*.

Assuming legislation is passed and the reforms commenced, the new processes would be subject to ongoing monitoring to ensure they operate effectively. We will consider options, including post-implementation review, following the commencement of the new processes. The Government will continue to engage with stakeholders to determine the effectiveness of the new processes.

Regulatory burden estimate (RBE) table

Average annual regulatory costs (from business as usual)				
Change in costs (\$ million)	Business	Community organisations	Individuals	Total change in cost
Option 1	\$0	\$0	\$0	\$0
Option 2	-\$129	\$0	-\$36	-\$165
Option 3	-\$152	\$0	-\$40	-\$192

Annex 1: Submissions Received on Draft Primary Law

No.	Submission
1	SM Solvency Accountants
2	nem
3	Mr Chandrasegaran (Solicitor)
4	Vantage Performance
5	<i>Confidential</i>
6	Anequity
7	SV Partners
8	Jones Day
9	Turnaround Management Association (TMA)
10	Australian Small Business and Family Enterprise Ombudsman (ASBFEO)
11	Property Council of Australia
12	Mr McKillop (Barrister)
13	Dr Mogg (Researcher)
14	DW Advisory
15	Australian Finance Industry Association (AFIA)
16	Financial Counselling Australia (FCA)
17	CA ANZ
18	Association of Independent Insolvency Practitioners (AIIP)
19	Southern Steel Group
20	Grant Thornton
21	Business Law Section of the Law Council of Australia (Law Council)
22	Barret Walker
23	Mendelsons Lawyers and Prushka Fast Debt Recovery
24	Australian Restructuring Insolvency & Turnaround Association (ARITA)

25	KPMG
26	Shopping Centre Council of Australia (SCCA)
27	Dye & Co
28	Worrells
29	Mr Wellard (Academic)
30	Australian Institute of Credit management (AICM)
31	Mr Arbogast (Barrister)
32	Australian Banking Association (ABA)
33	The Institute of Certified Bookkeepers
34	Australian Institute of Company Directors (AICD)
35	MinterEllison
36	MCorp Advisory
37	Australian Chamber of Commerce and Industry (ACCI)
38	Pitcher Partners
39	<i>Confidential</i>
40	<i>Confidential</i>
41	Mr Harris (Academic)
42	DLA Piper
43	McGrathNicol
44	Mr McDonald (Barrister)
45	Mr Eskdale (SME Adviser)
46	Mr Brown (Academic)
47	Institute of Public Accountants (IPA)
48	Australian Credit Forum (ACF)
49	CPA Australia
50	Mills Oakley

Annex 2: Submissions Received on Draft Regulations and Rules

No.	Submission
1	Shopping Centre Council of Australia (SCCA)
2	Mr McDonald (Barrister)
3	MinterEllison
4	Australian Institute of Company Directors (AICD)
5	Business Law Section of the Law Council of Australia (Law Council)
6	DCA Group
7	Chartered Accountants Australia and New Zealand (CA ANZ)
8	Australian Restructuring Insolvency and Turnaround Association (ARITA)
9	NSW Small Business Commissioner
10	Australian Credit Forum (ACF)
11	Australian Banking Association (ABA)
12	Mr Wellard (Academic)
13	<i>Confidential</i>
14	CPA Australia (CPA)
15	Institute of Public Accountants (IPA)
16	Australian Finance Industry Association (AFIA)
17	<i>Confidential</i>
18	Property Council of Australia (Property Council)
19	Australian Institute of Credit Managers (AICM)
20	Australian Small Business and Family and Enterprise Ombudsman (ASBFEO)