PPB ADVISORY

Our Ref:SDP:ILRB14 Submissions

19 December 2014

Manager
Corporations and Schemes Unit
Financial System and Service Division
The Treasury
Langton Cresent
PARKES ACT 2600

By Email insolvency@treasury.gov.au

Dear Sir

Submissions Exposure Draft Insolvency Law Reform Bill 2014 and Insolvency Practice Rules Proposals Paper

We enclose our submissions set out in the following order:

We consider that if the changes recommended in Part A are not made the expected savings to the costs of insolvency administrations will not be realised and the costs of administration will actually increase.

We consider the changes requested in Part B will further enhance efficiency benefits from those reforms.

We would be delighted to provide any further information or clarification at your convenience.

Yours faithfully

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Partner

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Part A

Trustee must not derive profit or advantage from administration of the estate

Insolvency Practice Schedule Section 60-20 (4)(c)(ii)

Submission: Insert 60-20 (4)(c)(iii) "the person is the disclosed practice entity"

Requiring creditor consent before engaging the EA's own Practice entity to perform work on the administration is impracticable, inefficient, anticompetitive and will frustrate EAs from performing their duties.

In most modern practice structures all staff (often including EAs), computer and office equipment, stationery and office supplies are provided by a related entity. This is true for practices run as companies, trusts, partnerships and even many sole practitioners.

To avoid committing a strict liability offence in every appointment, EAs will need to immediately convene a meeting of creditors to seek consent to engage the EAs firm. However even doing this will be an offence as staff and expenses will be incurred convening and holding the meeting.

The alternative is only sole practitioners trading in their own name will be able to undertake administrations. Proper resources and expertise cannot be brought to an assignment if all EAs are sole practitioners.

If creditor consent can be obtained retrospectively (inconsistent with strict liability) a meeting of creditors will still be required in every estate (including small and assetless) which would have the effect of eliminating any advantage from introducing the "maximum default amount" under Section 60-15 and overall will increase the costs of administering administrations.

EA's Practice entities are recorded at ASIC/ASFA on firm letterhead and websites. The law can simply require these details to be disclosed and searchable with those enitities exempt from section 60-20.

Funds Handling
Insolvency Practice Schedule Division 65

Submission: Remove strict liability offences and allow EAs to defend prosecution where they have sufficient reason.

Strict liability offences in Sections 65-10, 65-15, 65-20, 65-25 and 65-40 are draconian penalties for small administrative errors where there is no intent to by the EA to act dishonestly or cause loss. The EA may be prosecuted for the actions of unrelated third parties.

Strict compliance systems will be unable to prevent all instances of error exposing EAs to significant risk of prosecution and fines disproportionate to any loss suffered. Examples of the types of unintentional errors which could occur are contained in Schedule 1 below.

The Explanatory Memorandum does not explain the justification for applying strict liability offences as required by the "Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers".

Pursuant to Section 65-25, the Court may remit penalty interest (20% per year) if the Court is satisfied the trustee had sufficient reason for failing to comply. This power is inconsistent with a strict liability offence for the same conduct which will apply regardless of sufficiency of reason. The fine of $5,500 will in most cases exceed the penalty interest.

50 penalty units is double the current penalty for directors' failing to lodge a RATA (or equal to after Act commences). Failure to lodge a RATA has a far more detrimental effect to efficiency in insolvency administrations than minor clerical errors.

PPB Advisory presently has more than $600 million of funds held for insolvency administrations and processes approximately 4,000 receipt and payment transactions every month. An error rate of one mistake in every 1,000 transactions (of the types outlined in Schedule 1) would result in annual fines of $264,000 per annum.

We can think of no other profession or vocation where penalties for administrative and unintentional errors are as severe.

Part B

Reasonable Requests for Information and Reports

Insolvency Practice Schedule Sections 70-40, 70-45, 70-50, 70-56, 80-40

Submissions: Clarify which Rule applies to requests which are both reasonable and unreasonable; provides requests are unreasonable if made within 60 business days of a previous request; and a new ground, if made by a regulated debtor who had not filed a SOA.

The Proposed Insolvency Practice Rules definitions for reasonable and unreasonable requests for each of the above provisions appear to be identical and are largely unhelpful. It is conceivable that many requests for information will be both reasonable and unreasonable, for example a request for work in progress records in an assetless matter, in which case, which Rule will apply?

10 business days between requests is far too short. Only a voluntary administration is likely to change materially during a two week period however in that case the "will shortly be provided to creditors in another document" exception would usually apply. 60 business days is a reasonable timeframe for a reasonable request.

Regulated debtors' requests should be automatically unreasonable where they have failed to comply with an obligation to file a SOA.

Resolution definition

Insolvency Practice Rules paragraph 155.

Submission: Ordinary resolutions for all EAs be defined as a majority in value whether at a meeting or without a meeting.

It is proposed that a Resolution without a meeting will be passed by a majority in number of creditors voting. This changes the voting for regulated debtors which are presently resolved by a majority in value. There is no explanation for this change in the Explanatory Memorandum.

In our opinion it is easier for a small group of related creditors to influence the outcome of administrations to the detriment of large unrelated creditors.

Creditors Meetings continue to require majority in number and value (with casting vote) accordingly the same resolution put to a meeting may result in a different outcome to a resolution without a meeting. This undesirable outcome is not presently possible under the Bankruptcy Act.

Paragraph 155 of the Insolvency Practice Rules refers to Corporations Regulations 5.5.19 which does not exist.

Transfer of books to new EA
Sections 70-30

Submission: 10 business days is appropriate. Clearly define "books" to be transferred.

The five business time limit does not take account of the practical implications of a change of EA. Whilst the new EA's appointment takes effect immediately, the former EA still has obligations to finalise the former appointment including paying expenses and liabilities for which the EA is personally liable and closing the bank account etc.

As non-compliance is an offence, a precise definition of records required to be transferred is required. The exposure draft unhelpfully contains many expressions relating to records including: proper books (70-10), any books relating to the administration (70-25, 70-30, 70-31), all books that relate to the administration (70-35(1)) and any books that the regulated debtor has given to the trustee (70-35(3)).

Creditors may request meeting to establish committee of inspection
Insolvency Practice Schedule Section 80-5

Submission: Insert into Section 80-5(1) "subject to Section 75-15"

It appears a single creditor can request a meeting of creditors without the restrictions otherwise proposed by section 75-15. This will defeat the intention of section 75-15 and result in increased costs of administration.

Court may inquire on application of creditors etc.
Insolvency Practice Schedule Section 90-10

Submission: A regulated debtor can only apply for an enquiry if the debtor has a financial interest in the estate.

Trustees are often submitted to fruitless and unsuccessful litigation by regulated debtors where there is no prospect of recovering costs in small and assetless estates.

Court may make orders in relation to estate administration

Insolvency Practice Schedule Section 90-15

Submission: Applications for review of EAs decisions must be made within 60 days of becoming aware of the relevant decision.

Section 178 of the Bankruptcy Act (which is to be repealed) provides that trustee's decision may only be reviewed within 60 days of becoming aware of the decision. This important limitation facilitates trustees complying with their (Section 19) duty to administer the estate as efficiently as possible by giving the trustee certainty relating to past actions and avoiding frivolous claims.

No time limit is proposed under Section 90-15 nor is time a factor the Court may take into account under 90-15(4).

Part C

Committee of Inspection may obtain specialist advice or assistance

Insolvency Practice Schedule Section 80-50

A Committee of Inspection can only obtain specialist advice with the approval of the EA. If approval is not given, is it intended this will be reviewable by the Court under Section 90-20?

Removal by Creditors

Insolvency Practice Schedule Section 90-35

The guidance on what may constitute an improper removal is unhelpful to combat abuse of these provisions.

Insolvency Law Reform Bill 2013 – Director Disqualification.

We are disappointed that the director disqualification provisions proposed in the previous version of this Bill have been abandoned.

The RATA is an important document to enable efficient conduct of EAs with a low compliance rate. The penalty for non-compliance is to be raised to 50 penalty units which still seems inadequate given the penalties to be applied to EAs for funds handling errors or disbursements by a related entity.

Registration and Discipline of EAs

We support the introduction of Committees for the registration and discipline of liquidators. We are aware of ARITA's submissions and support the changes sought by ARITA.

Annual Estate Returns

Insolvency Practice Schedule Section 70-5

We note that trustees must lodge annual estate returns with 25 working days, however company EAs have 3 months to lodge an annual administration return.

We submit they should be aligned at 3 months.

ASIC/IG may direct EA to comply with the request for relevant material.

Insolvency Practice Schedule Section 70-70

Submissions: EA should have a right to review to decision of ASIC or the IG.

Amendments Consequential on the Introduction of the Insolvency Practice Schedule

Items 26-29.

Substantial changes to Bankruptcy Act Section 73 are consequential on moving meeting procedures to the Insolvency Practice Rules. However the removal of Section 73(2) appears to result in the bankrupt having no authority to cause the trustee to convene a meeting. The bankrupt is not a person eligible to require a meeting under Section 75-15. Is that an intended consequence?

Review

Insolvency Practice Schedule Section 90-26

What is the prescribed period pursuant to Section 90-26(4)(d)? EA's remuneration should only be able to be reviewed within a reasonable period of time.

Amendments consequential on the introduction of the Insolvency Practice Rules (Corporations)

Item 137 After Section 477(2B)

Is this amendment intended to apply to payments of expenses made by way of indemnity (that is, they can be recovered from the company if it subsequently realises assets), such as for litigation? Such intention should be express if it is intended.

About PPB Advisory

PPB Advisory is a firm of professional advisors employing more than 300 people (including 4 registered trustees in bankruptcy and more than 30 registered liquidators) with offices in Sydney, Melbourne, Brisbane, Perth and Auckland. Approximately three quarters of the firm is engaged in providing insolvency services and related advice.

We have previously made submissions in relation to the Options Paper, Proposals Paper, ILRB2013 which preceded this Exposure Draft.

Abbreviations used in this submission

EA	External Administrator
EFT	Electronic funds transfer
IG	Inspector General in bankruptcy
RATA	Report as to Affairs
SOA	Statement of Affairs
Other Abbreviations	As per Explanatory Memorandum

Schedule 1

Examples of funds handling errors

Deposit by Electronic Funds Transfer (EFT)

EAs have no role to play in the deposit of funds to an administration account by EFT. Debtors, customers and other payees may wrongly deposit administration funds to the EAs firm, trust account or wrong administration. Government departments frequently make deposits to incorrect administration accounts. Payments could deliberately be paid by a third party (for example a regulated debtor or company director) in order to induce an offence by the EA.

Pre-Appointment bank accounts

It is common practice for appointments to trading businesses for the EA to retain the business' pre-appointment account on a 'credit only' basis to minimise disruption to customers, retain credit card facilities and/or maximise cashflow. This would be an offence (65-10) even if the funds were swept to the administration account within 5 days.

Joint and Several Estates, Related but unpooled companies

Cheques or other receipts containing funds for more than one administration cannot be banked to any individual administration and then appropriately split, this would be two offences (65-15 and 65-25). The law about joint and several estates is antiquated and complicated. EAs, their advisors and the IG often differ in their interpretation of this law. A trustee who is mistaken as to the correct estate will be guilty of an offence.

Income versus Asset

Except in the case of barristers, Bankruptcy Law is unsettled as to whether pre-appointment trade debtors constitute an asset of a bankrupt estate or income of the bankrupt subject to the income assessment regime. A trustee who banks a debtor to the administration account which subsequently turns out to be income will commit an offence (65-15). If a regulated debtor retains a debtor or other receipt which turns out to be an asset, the trustee will commit an offence (65-10). This will be so even if the regulated debtor does so deliberately, dishonestly or otherwise without the trustee's consent.

Disputed Funds

Funds may be paid to an administration under protest, subject to a claim, trust or purported trust. This may include express, constructive or resulting trusts and matrimonial claims. The EA will commit an offence if he deposits disputed funds that are found not to be property of the administration (65-15) or if he does not deposit funds which are subsequently found to be property of the administration (65-10).

Double paid invoice

Some bank's EFT systems allow double processing of the same payment. Even if this mistake is detected immediately and double payment reversed or refunded, an offence will be committed.

False Creditor Claim

Paying a dividend to a creditor whose claim is found to be false or overstated would be an offence by the EA. A fraud committed on the estate by a staff member would be an offence of the EA.

Withholding Tax

Where a bank incorrectly deducts withholding tax from a regulated debtor's estate the trustee will commit an offence (65-25) The trustee commits an offence where a bank makes a mistake with a deposit by crediting the wrong account.

Opening Account

Where a bank fails to open a bank account within five days of receipt of the first receipt of the administration, even if the cheque has been delivered to the bank for deposit.