POLICY & CORPORATE AFFAIRS

POLICY BULLETIN

DATE: 9 March 2018

1.0 CPA Australia gives evidence to Bankruptcy Amendment Bill inquiry

CPA Australia's Policy Adviser - ESG, Dr John Purcell FCPA, gave evidence this week to the Senate Legal and Constitutional Affairs Legislation Committee inquiry into the Bankruptcy Amendment (Enterprises Incentives) Bill 2017.

The central plank of the proposed reform is to reduce the amount of time that must pass before a person is automatically discharged from bankruptcy, from the current three years to just one year.

CPA Australia's position is that we do not support reducing the bankruptcy default period to one year as the current three-year period achieves balanced outcomes for the various interests at stake. The rationale for our position is as follows:

- Reflecting the views of CPA Australia members who have provided comment to the Policy team, such reform may dissuade individuals from pursuing available and effective means of meeting financial obligations engendering an attitude of seeking a 'quick fix'.
- The proposal unduly risks further altering the balance of creditor and debtor interests within Australian law which has typically, though not excessively, favoured the former.
- It is emphasised that the proposed reform is not presented from the perspective of unfairness or injustice, rather economic incentive the effect of which can be effected by a much wider range of factors.
- The reduction of the default period is necessarily accompanied by a number of 'anti-abuse' type measures such as those dealing with income contribution and scope for Official Receiver objections, which potentially add cost to the overall administration of the bankruptcy scheme.
- The demographics (age, occupations etc.) and causes of personal bankruptcy detailed in the Australian Financial Security Authority's extensive statistics strongly suggest that these laws do not directly touch the behaviour of the intended cohort of potential science/ tech. innovators or would-be entrepreneurs, and is thus, misdirected.

Given the possibility that the government will persist in implementing this fundamental change, we have suggested that any legislation giving this effect be accompanied by a requirement for an independent review after two years of operation, as is the case with the introduction of insolvent trading reforms under the Corporations Act.

For further information, the Hansard transcript of Dr Purcell's evidence is attached.

Yours sincerely

Stuart Dignam
General Manager – Policy & Corporate Affairs

COMMONWEALTH OF AUSTRALIA

Proof Committee Hansard

SENATE

LEGAL AND CONSTITUTIONAL AFFAIRS LEGISLATION COMMITTEE

Bankruptcy Amendment (Debt Agreement Reform) Bill 2018, Bankruptcy Amendment (Enterprise Incentives) Bill 2017

(Public)

TUESDAY, 6 MARCH 2018

MELBOURNE

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[PROOF COPY]

WITNESSES

CULL, Mr Innis, Senior Manager, Pitcher Partners

DOWNEY, Mr James, Private capacity

FORD, Ms Melissa-Jane, Principal Legal Officer for Private International Law & Commercial Policy, Civil Law Unit, Attorney-General's Department

GIASOUMI, Mr Nicholas, Director, Dye & Co. Pty Ltd

JOHNSON, Mr Michael, Assistant Secretary, Civil Law Unit, Attorney-General's Department

LEECH, Mr Peter, Chair of the Insolvency and Reconstruction Committee, Business Law Section, Law Council of Australia

LHUEDE, Mr Michael, Private capacity

MEARNS, Mr Clifford, Director, SRMC Limited

MENDELSON, Mr Roger Glave, Chief Executive Officer, Prushka Fast Debt Recovery Pty Ltd

PARIS, Mr Benjamin, Registered Debt Agreement Administrator, DCS Group

PURCELL, Dr John, Policy Adviser ESG, CPA Australia

RAMBALDI, Mr Gess, Partner, Pitcher Partners

ROZEA, Ms Jennifer, Private capacity

RUHE, Mrs Alice Fay, Partner, SellersMuldoonBenton

PURCELL, Dr John, Policy Adviser ESG, CPA Australia

[10:15]

CHAIR: Dr Purcell, thank you very much for joining us. These proceedings are proceedings of parliament, and parliamentary privilege applies. There are provisions relating to protection of witnesses. I don't really think they are relevant in this particular inquiry, but I understand we have given you information on those things in any case. We do have the CPA's submission. Thanks very much for that. We ask you to make a short opening statement and then we'll ask you a couple of questions.

Dr Purcell: I thank the committee for the invitation to appear here today representing CPA Australia. In simple terms, bankruptcy and insolvency laws involve a formalised process of collecting and liquidation of a debtor's available assets, from which a rateable distribution is made to creditors. Our present laws of personal and corporate insolvency have evolved over many centuries and demonstrate a range of shifting emphases. Perhaps most notably, over time, the rehabilitative purpose has become increasingly important, at least as important as the deterrent and punitive aspects, if not more so.

Essentially, however, the underlying reality of bankruptcy law is a resolution of competing claims to private law entitlements within a public law setting where an insufficiency of assets prevents enforcement of all claims. As such, the law seeks to strike a balance, though invariably an imperfect one, between the interests of debtors and creditors. Any substantive law reform, such as that contained in the bill before the committee, potentially alters this balance, and, because of the complex nature of the statutory instrument, can be prone to cause unintended consequences. CPA Australia thus urges caution in the development and implementation of the reforms at hand.

The enterprise incentives bill currently before the committee has its origins in the April 2016 proposals paper entitled *Improving bankruptcy and insolvency laws* developed under the National Innovation and Science Agenda. The committee will be aware that key corporate insolvency law reform proposals included addressing the more punitive operations of ipso facto clauses by creditors, where a debtor company might reasonably be seeking to restructure, and introducing a safe harbour for directors against personal liability, where, broadly, a course of action had been developed which was reasonably likely to lead to a better outcome for the company.

Perceptions as to the harshness of Australia's corporate insolvent trading rules vary widely, and reforms now in place are controversial. Moreover, the economic-outcomes character of the changes in section 588G of the Corporations Act may bring with them indeterminacy as to their true effect. As such, the new safe harbour course of reasonable action defence in section 588GA is accompanied in section 588HA by an independent review requirement to be initiated by the minister and undertaken as soon as practicable two years after enforcement. Given the significant changes that were brought about by the bill now before the committee and the speculative character of the asserted economic benefits, CPA Australia urges that, were the reforms to proceed, there be built into the Bankruptcy Act a similar independent review process.

I turn now briefly to the economic intent underlying the enterprise incentives bill. The proposed reforms are not presented from a social perspective of achieving greater fairness and ameliorating hardship but rather from an economic rationale of enabling entrepreneurial behaviour and removing the stigma of bankruptcy. We've raised in submissions to both the committee and to Treasury concerns as to the mooted causal relationship between the central plank of the reform, that of the addition of section 149(5) setting the bankruptcy discharge period of one year after filing a statement of affairs, and an assumed willingness on the part of a bankrupt to re-engage in business or the community more broadly to contemplate entering business activity accompanied by a reasonable level of risk.

The Australian Financial Security Authority statistics on the causes of bankruptcy and the characteristics of debtors are such as to prompt significant caution in pursuing this reform. Moreover, it is remarked that the frequency of personal insolvency is affected by prevailing economic conditions and structural change. It is important thus to consider how these changes will operate in both upswings and downswings in economic cycles and thus how attitudes around the ease of exiting existing obligations with a view to a fresh start would be influenced. Similarly, the referred deregulatory influence benefits ought, CPA Australia believes, be assessed over an extended period beyond the foreshadowed one year's saving, particularly as the significant consequential changes, such as those dealing with income contribution will take some time to have an economic impact reasonably capable of substantiation.

To conclude, given absence of definitive empiricism and wide societal consensus that Australia's personal insolvency and bankruptcy system is flawed in its social consequences and in the achieving of as fair as possible outcomes for debtors and creditors, the bill should be accompanied by the review process we've urged. I will be pleased to now address any questions the committee has.

CHAIR: Thanks very much, Dr Purcell. We seem to have a two-page submission from CPA which is nowhere near as detailed as your submission. That could be because our procedures have not caught up with another submission or—

Dr Purcell: These are additional remarks that I'd like to present to the committee.

CHAIR: If that's in written form, would you be prepared to table that as a further submission?

Dr Purcell: Yes, most definitely. I'm pleased to do so.

CHAIR: I think the committee could agree to accept that as a further submission.

Senator PRATT: That would be great.

CHAIR: We'll get that from you later then. I notice that, in your initial statement—and I appreciate that this is broad—you indicated that CPA does not support the passage of the bill. As I was saying before, I have some unease, having been 100 years ago a small town country legal practitioner, that this seems to me to be focused on looking after the ones who have gone bankrupt and not enough on those who have actually lost the money as a result. But we've had quite a bit of evidence from a number of sources—most recently, the previous witnesses—who are suggesting that we should divide the one-year discharge or confine it to the good guys, the people who are honest bankrupts, and exclude the bad guys, such as the Christopher Skases of this world, and define two different approaches. Do you have any comment on that?

Dr Purcell: At some level, it would have merit, but, in terms of how you would implement such a two-tiered approach, I wonder as to the level of complexity that you are building into a system at present which is not manifestly broken. I think it would call into question the need for a significant level of analysis by both public practitioner accountants in the first instance and then insolvency practitioners and trustees in bankruptcy, to actually ascertain which particular party would fall into the category that ought be encouraged through the benefits of the one-year period as opposed to those who should be subject to more vigorous application of laws against the prohibitions of their continued business activity.

CHAIR: And that's a concern the committee has had as well, in terms of how you define that and how you separate and distinguish them, although people who are day by day in practice in this area seem to think that it is possible and that there are different parts of different law that have these same distinguishing—

Dr Purcell: I would say that any form of law reform of this nature, which initially has an economic motivation to it, does have social consequences attached to it and has the potential to affect the balance between creditor and debtor interests. It's on that basis that, in my introductory remarks, I said that, if the reforms were to proceed in some form, they ought be accompanied by a review process which will allow sufficient time to gauge the impact but then to be able to assemble the right level of empiricism to see whether in fact the desired economic outcomes have been achieved and to ensure that there have been no significant downturns from a social and debtor-creditor relationship prospective.

CHAIR: Sorry, Dr Purcell, we didn't clarify with you: are you a practitioner yourself or are you an officer of the CPA organisation?

Dr Purcell: I'm an officer of CPA Australia working in the policy area.

CHAIR: And you have a group at the CPA that is particularly interested in this sort of—

Dr Purcell: As we have alluded to in our short submission to the committee, we have canvassed the views of some of our members in public practice. I'll hedge this by saying it is not deep, comprehensive analysis of a wide range of accountants in practice. Nevertheless, among those who have come forward on the invitation to comment and have input into what we say to the committee in relation to this bill, there are significant concerns about the effect on the deterrent aspects associated with the Bankruptcy Act. None of us wish to see a body of laws which are excessively punitive, but there are both social consequences associated with bankruptcy obviously and it does send significant messages about both the conduct of business behaviour and how an individual respects his private law obligations, particularly at contract.

CHAIR: I think your members who you have canvassed are of my general view. I started off sharing that, but I accept that my government's approach to encouraging entrepreneurship might need to be slightly different. I appreciate what you've said and I understand where your members are coming from. Senator Pratt, do you have some questions?

Senator PRATT: You raise the point of view of unsecured creditors in this. What can we learn from their views? Clearly, being an unsecured creditor means you're working for nothing if you're a supplier to someone who is not paying their debts.

Dr Purcell: And again, the view coming from that small group of members that we've been able to engage with on this matter is that they feel potentially vulnerable in these particular regards.

Senator PRATT: Do they feel particularly vulnerable because they're worried about repeat behaviour and wanting to protect other people from this situation if people are phoenixing companies and they do this again? Or do they want to get their pound of flesh, in terms of a length of bankruptcy to punish people? Where are they coming from?

Dr Purcell: As a small-business person, your public practitioner accountant will work with critical understanding of where the cash flow sits. There will be a legitimate creditor interest in ensuring that laws in relation to bankruptcy operate in such a manner which is not going to penalise them as practitioners providing a service. They are also, I would urge, concerned about knock-on effect behavioural—

Senator PRATT: In a sense you're arguing that the current bankruptcy regime, the stigma and the length of it act as a disincentive to people accumulating too great a level of debt, and your members are worried that these actions will open a floodgate for poor behaviour because the penalties aren't great enough.

Dr Purcell: I appreciate the previous evidence which has been given about the potential of splitting into different categories. Nevertheless, our public practitioner members, who we've engaged with, expressed the view that if this change is to take place there is a greater incentive not to honour one's debts and an undue expectation that one can stand out of normal commercial trading obligations for a shorter period in anticipation of being able to start afresh.

Senator PRATT: The bill doesn't currently have this provision, but you've heard some of the evidence this morning about a much closer audit of prescribed behaviour before you could be lifted from that. Is that something you would support?

Dr Purcell: We would support that. I don't wish to be seen as excessively negative in relation to the matters which can be put in place to ensure that the reform is not subject to abuse but, any additional oversight, either through the official trustee or registered trustees, is going to add additional regulatory costs associated with it in terms of supervising and assuring that those potential abuses are minimised.

Senator PRATT: Three years seems too long to the government at the moment and so they're reducing it to one year. In the views of your members, is three years enough? What do you want to have done to bankrupts? Do they deserve a chance to try again?

Dr Purcell: It would be a very harsh person who would say that an individual does not deserve a second chance. CPA Australia and its members would not wish to see a law excessively punitive in nature. Nevertheless, as the bill stands, it doesn't have those checks and balances built into it and it doesn't have a review process in it that we would urge. I think it requires a degree of rethinking. Understandably, the UK operates with a one-year period and New Zealand has a three-year period. It needs to be demonstrated that we are not inviting undue negative consequences.

CHAIR: Dr Purcell, do you have any experience with the UK situation? Have there been problems there that you're aware of?

Dr Purcell: Not that I'm aware of, but I would happily go away and research—

CHAIR: I guess we can google it ourselves these days, but are you aware of other jurisdictions where a shorter period has been provided?

Dr Purcell: I would expect that the USA operates with a shorter period, but comparisons between Australia and the USA in relation to both corporate and individual bankruptcy is very difficult. Your nearest comparisons are obviously going to be, I would say, the UK and New Zealand.

CHAIR: Thanks very much for your time and for the input from your members. We appreciate every bit of support we can get in looking at this and trying to see if the government's on the right track or whether some amendments are needed, so thanks very much for your help.

Proceedings suspended from 10:35 to 11:01

RESOURCES

Policy & Corporate Affairs – Professional Resources

CPA Australia continues to represent its members and has an ongoing relationship with key regulatory, statutory and professional standards bodies.

Current consultations and CPA Australia policy submissions can be found at: https://www.cpaaustralia.com.au/media/consultations-and-submissions

Other professional resources can be found at: https://www.cpaaustralia.com.au/professional-resources

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