ON THE BEAM

CONDON
FORENSIC INSOLVENCY TURNAROUND
ASSOCIATES

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Welcome To 2013, Who's Got Their Hand in My Pocket This Time?

By Schon G Condon RFD

Well welcome to 2013 a year that I am confident will be full of novel and interesting challenges that will be peculiar to the new environment in which we operate. The most important thing to remember is that it is a year in which we must learn from the change that is continually occurring around us.

The Global Financial Crisis (GFC) is not yet over, in fact the reality of its overall and sustainable solution is yet to be identified and applied. More importantly it will be both the global acceptance of change as well as its implementation. Recent events have also indicated that remote significant commercial operations are clearly to be one of the new targets and the issues and costs that will impact business will likely be significant, particularly from a cost perspective.
In addition to all of this you have the questioning of the commercial sustainability model of our current economic system by the likes of Dick Smith and others.

Clearly an interesting time to be in business.

One thing however that did catch my interest before Christmas was a brief note that was issued by the *Argyle Partnership, Solicitors* relating to superannuation. As Insolvency Practitioners, and in particular Trustees in Bankruptcy we are well aware of the importance of the protection of an individuals' superannuation funds i.e. the funds real value. Categorically the Bankruptcy Act enshrines it, regardless of the balance of an individuals' superannuation balance, the funds are simply not available as an asset available to creditors in a Bankruptcy to meet their claims. The simple logic behind this approach is that the Government is seeking to ensure that it is the individual that will fund the burden of their retirement not the Government.

In the light of this it is quite amazing therefore that, as the Argyle notice indicates, the Commissioner of Taxation has issued an instruction to its collection area that the garnisheeing of a Taxpayers Superannuation Funds for the purpose of recovering debts owing to the Commonwealth (including personally guaranteed corporate debts) is both legal and to be actioned. The sleeping time-bomb in this plan is the Directors liability for Superannuation Guarantee Charges after three months, an ill-prepared or ill-advised Director may well find that his efforts in personal financial planning have been futile as their super fund is decimated to fund the unpaid entitlements of their staff. A situation' with proper planning and action that could have been avoided. Beware the practitioner that fails to alert the Director, as once the Directors superfund is lost it is quite likely that the Director will search out and look to someones professional indemnity insurance to reinstate it!

As I said at the start, 2013 will be a great year in which we can all do some learning. Let's just make sure we don't have to pay excessively for the lesson!!

Have a great year, enjoy it and I do hope you enjoy our newsletters, but most importantly have fun!

Inside this issue:

Directors and "Directors" – Part 4 (Defences to an Insolvent Trading Action)

By Brandon Lee

In our November 2012 issue of "On The Beam", I discussed issues relating to the Directors' duties to prevent Insolvent Trading pursuant to Section 588G of the *Corporations Act 2001 (Cth)* ("the Act").

Recently, the growth in the number of Insolvent Trading offences reported have led to a trend to make Directors

proportion" to the prejudice to the company's creditors.

The Court of Appeal's decision may have far-reaching implications. Tenants should consider the possibility that their leasehold interest could be extinguished by a liquidator's disclaimer. Other parties affected may also include financiers of businesses operating from leased premises, as they may consider adjusting their lending criteria to reflect the risk of disclaimer.

It should be noted that an application has been filed with the High Court of Australia to challenge the Court of Appeal's decision. It will be interesting to follow any further developments on this topic.

Important Facts about Your Credit File!

By Sadia Alam

Section 18 E (1) and Section 18 E (2) (a to f) of the Privacy Act 1988 (Cth) provides for the storing of information in regard to your credit report and outlines what information is permitted to be stored.

When applying for credit, you can be certain that your selected Lender will most definitely perform a thorough check of your Credit File to validate your ability in making payments as and when they fall due.

Some important facts to keep in mind regarding the length of time at which information is stored on your Credit File is provided below;

In a case where you have been subject to a Court Writ or Summons (official notice issued from Court), information is kept for four (4) years on your Credit File.

Where there is an activity such as a Credit Enquiry/Inquiries i.e. where you seek to gather information regarding the availability of funds without disclosing your identity, or advising on the amount of funds to be borrowed, or failing to provide the details of your Credit Worthiness, this information is kept on your Credit File for a period of five (5) years.

A period of five (5) years also applies to a situation where a Court Judgement (i.e. a document issued by Court that contains information such as the amount of the debt, plus costs and interest, starting from the date of the Court proceedings you owe to the Creditor) or a case of Payment Default (lists of overdue payments in your name) is made against you.

In the event of Bankruptcy, a Part 9 Debt Agreement (where all existing debts are consolidated into the one debt), Part 10 Personal Insolvency Agreement and a Clear Out (also called a serious Credit Infringement where the Credit provider has tried to locate you unsuccessfully and believes to a reasonable degree that you have decided to not pay the debt), information is kept on file for a period of seven (7) years.

In the case of Previous Directorship and External Administration (winding up of a Company), the information is stored for a period of ten (10) years.

The above mentioned points are just some of the important facts to keep in mind when you seek to apply for finance or credit in the future.

Condon Update

The New Year brings new beginnings and in January we welcomed a number of new staff members to the Condon Group. Jon Gillingham was the Executive Manager at a major commercial bank; his experience will bring a brand new perspective to the Group. We look forward to developing new and existing relationships with Jon.

Jack, Sophie and Irma joined the Group at the end of January as Graduate Accountants. We are excited to be guiding and developing them as they embark on their insolvency careers.

In other news, congratulations to Schon for winning the Hole in one trophy at the War Memorial Trophy Golf Day.

The newest members of the Condon Group family- Jack, Sophie, Irma and Jon.

Jason Li presenting the "Hole in One" trophy to Schon.

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more responsible for their Company's contravention of Section 588G of the Act. Nevertheless, Section 588H of the Act provides a number of defences available to Directors against whom an Insolvent Trading action is brought. These defences will be discussed in this issue of *"On The Beam"*.

Under Section 588H of the Act, Directors can avail themselves of one of the four Statutory Defences listed under that Section and can be absolved from the Liability if they:

1. Had reasonable grounds to expect, and did expect, that the Company was solvent and would remain solvent even if it incurred the debt, or incurred a range of debts including that debt.

   This requires Directors to prove that they had an actual expectation of solvency and the existence of reasonable grounds for that expectation;

2. Had reasonable grounds to believe, and did believe, that the Company was solvent and would remain solvent on the basis of information provided to them by a competent and reliable person responsible for providing adequate information about the Company's solvency.

   This requires the Directors to prove that they relied upon information regarding the solvency of the Company provided by a competent and reliable person which led to an expectation of the actual solvency of the Company. Directors need to show that reasonable inquiries were made of matters that were not understood at the time and that further information was requested of that reliable and competent person.

3. Did not participate in the management of the Company at that time because of illness or other good reason.

   To succeed with this defence, there must be a nexus between the non-participation and the 'good reason', more so if illness was not the reason for non-participation. Distance and time zones are generally not adequate reasons for not being aware of the Company's position. Directors have to prove that they were incapable for the entire period under review.

4. Took all reasonable steps to prevent the Company from incurring the debt. Matters that may be considered when determining whether this defence is available include, but are not limited to any action Directors take to appoint an Administrator to the Company, when that action was taken and the results of that action.

   It should be noted that the onus is upon the Directors to prove this defence and not for the Liquidator or Administrator to disprove an assumption that a defence is available.

In addition to the defences listed under Section 588H, the Court can relieve Directors from contravention of Civil Penalties if he or she has acted honestly and ought fairly to be excused, as provided for in Sections 1317S and 1318 of the Act.

In conclusion, the abovementioned defences may seem useful and easily applicable but in reality the Courts will ultimately look to the legislative intent of the Insolvent Trading Provisions when considering the availability of a defence. It is therefore clear that the Courts have interpreted these defences in a fair and restrictive manner to remind Directors of their responsibility to avoid Insolvent Trading.

ASIC issued a Regulatory Guide 217 Duty to Prevent Insolvent Trading: Guide for Directors (RG 217) in July 2010. It sets out key principles to help Directors understand and comply with their duty under s588G of the Act.

Fair Entitlements Guarantee

By Padmini Saheb

The Fair Entitlements Guarantee is the upgraded government scheme helping employees who lose their job and have outstanding entitlements because their employer goes into liquidation or is bankrupt. This scheme is run by the Department of Education, Employment and Workplace Relations.

From 5 December 2012, the Fair Entitlements Guarantee ("FEG") replaces the General Employee Entitlements and Redundancy Scheme ("GEERS").

GEERS will continue to operate for claims about unpaid entitlements from businesses that liquidated or went bankrupt before 5 December 2012.
Eligible employees may be able to get assistance through the Fair Entitlements Guarantee for:

- up to 13 weeks unpaid wages
- unpaid annual leave
- unpaid long service leave
- up to 5 weeks unpaid payment in lieu of notice
- up to 4 weeks unpaid redundancy entitlement per year.

The administration of claims under FEG will be largely the same as those associated with administering claims under GEERS except for the following keys differences:-

- Claims should be lodged no later than twelve (12) months after the Insolvency date;
- Claimants must be Australian Citizens or permanent residents or holders of special category visas;
- Unlike GEERS, under FEG there is no eligibility requirements relating to Deed of Company Arrangement and Personal Insolvency Agreements;
- Unlike GEERS, where entitlements are paid only up to the date of the appointment of an Insolvency Practitioner, FEG entitlements are paid up to the end of employment and simply reduced by the portion an Insolvency Practitioner is required to pay as a cost of winding up;
- The assessment of claims involving a transfer of business or employment to a new operator will be simplified from 1 July 2014; and
- Under FEG, claimants have a right to an external review by the Administrative Appeals Tribunal if they remain dissatisfied with a decision after an internal review has been undertaken by the department.

It is important to note that currently both Schemes do not acknowledge any excluded claims of the Directors and Related Parties.

Tenants' Leasehold Interest Vulnerable to Liquidators' Power to Disclaim Leases

By Maggie Lau

A liquidator is permitted by law to disclaim onerous property and contracts in a winding up to enable the company in liquidation to be free of onerous obligations so that it can be wound up without delay for the benefit of its creditors.

In August 2012, in the matter of *Willmott Forests Ltd (In Liquidation) [2012] VSCA202*, the Victorian Court of Appeal decided on a number of issues in relation to the power of liquidators as landlords to disclaim leases.

Willmott Forests Limited ("the company") went into liquidation and liquidators of the company sought to sell the company's land, which required clear title to the land. Therefore, the leases on the land were required to be terminated or extinguished.

The liquidators sought orders and directions from the Victorian Supreme Court as to whether or not they could disclaim the leases with the effect of extinguishing the leasehold estate or interest in the land.

In the first instance, the trial judge held that the liquidators could disclaim a lease under section 568(1) of the *Corporations Act 2001 ("the Act")*, but the lessees' leasehold interests continue to subsist.

One of the reasons for the trial judge's decision was that the disclaimer of the lease by the liquidator of the lessor only terminates the lessor's rights, interest and liabilities under that lease. Such a disclaimer *'would not bring the tenant's proprietary interest in the land to an end'*.

In addition, the company's obligation as lessor to ensure quiet enjoyment of the land by the lessees was not considered a liability or encumbrance on the property of the lessor. On that basis, it was not necessary to extinguish such an interest to release the lessor or its property from a liability.

The Court of Appeal overturned the trial judge's decision and held that on the termination of the interests of the lessee under a disclaimed contract, the leasehold interest is also extinguished.

The Court of Appeal examined the context of the word "liability" in the context of section 568D(1) of the Act, and formed the opinion that *"it should be given the widest possible meaning and include the obligation to provide possession and quiet enjoyment."*

In light of the above, the Court of Appeal then considered whether the leasehold interest remains even if the lease is disclaimed. The Court of Appeal noted that the purpose of Section 568 of the Act was to enable the company in liquidation to be free of obligations which would prevent the prompt and effective winding up of the affairs of the company, even if this may affect the rights of *"the most innocent of parties"*.

Furthermore, the Court of Appeal formed the view that any leasehold interest is governed by the contract of lease. Any leasehold interest cannot survive the termination of the very contract that created it and regulated the tenure of the lessees. Therefore, if the contract is disclaimed, the leasehold interest is also extinguished.

As a result of this decision, a liquidator of a landlord now has the comfort of knowing that upon disclaiming a lease, the land is no longer encumbered by a tenant's interest.

To compensate parties aggrieved by any disclaimer, the Act provides that they may claim to be a creditor and prove in the winding up of the company to the extent of the loss suffered because of the disclaimer. In addition, aggrieved parties may also apply to Court to set aside a disclaimer if they are able

to establish that the prejudice they will suffer is "*grossly out of*