14/5/2010

Mr Hawkins,

I live and work in regional Australia and have been involved with a number of insolvency practitioners over the past 5 years. Below are some of additional thoughts since lodging my Submission Number 52 in February this year and after reading other submissions received to date. I would like these thoughts to be taken into consideration when the committee considers any changes to improve the operation of the insolvency laws in Australia and would welcome an invitation to appear before the committee to discuss these proposals in more detail.

Damage to Regional Australia:

In most cases in regional Australia, insolvency practitioners are located hundreds of km away (in our case over 1000km) and creditors have no way to determine if the fees and charges are legitimate. It seems ridiculous to have someone so remote in charge of the realisation of assets to first pay himself and then pay the unsecured creditors if anything is left – this loophole needs to be addressed.

The damage caused to regional communities is often not taken into account by remote insolvency practitioners. Recently a private hospital in our town with over 100 beds was closed by a receiver following a power outage caused by a cyclone with a loss of numerous jobs and inconvenience to patients and the community in general. Once a business has been closed any goodwill instantly evaporates and it is costly for any potential new owner to restart.

In regional Australia it should be imperative that insolvency practitioners try to sell each business as a going concern. Despite our company's businesses being profitable, a bank appointed receiver closed 5 of the 6 businesses without trying to sell any of them as a going concern, sacking without notice over 97% of our employees who ended up being paid their entitlements under the GEERS scheme.

The subsequent fire sale clearance auctions of the floating assets (with a balance sheet value in excess of $1 million) realised considerably less than the fees and charges of the receivers, their lawyers, valuers and agents, resulting in a negative return to the bank and increasing the initial debt of $1.6 million to over $2.4 million after everything but the real estate had been realised. It would have been a far better result for all concerned if the receiver had just sent all the floating assets to the tip because at least they would have got something without having to incur all of the expenses. When I questioned the bank they said this was a result of the requirements in the Corporations Law.

Insolvency Levy to assist Directors and Unsecured Creditors:

It is not a good system where insolvency practitioners are required to take on 30% of their work for which they will not be paid. This means they have to overcharge by approximately 50% for the other 70% of their appointments which puts an unnecessary burden on companies who are already in financial difficulty.

The last thing a company in financial trouble needs is to have to foot the costs of an insolvency practitioner at $500+ per hour. In the first month of the receivership of our family company, the receivers charged over $147,000, even though they told us at the outset that the total cost would be around $200,000. The total cost was over $750,000 and we had no control over this.

I suggest that the Government legislate for ASIC to include an insolvency levy of $50 to $100 per annum in the annual registration fee for a company. This would provide up to $170 million per annum for ASIC and needs to be directed for the purpose of ASIC educating Directors on their responsibilities relating to insolvent trading and to carry out an initial investigation of a company in financial difficulty to faithfully report the true position of the company to creditors.

I was a Director for over 20 years and believed that because my company had a surplus of assets, this would meet my requirements as a Director in continuing to trade a seasonal business during the quiet time when customers were slow in paying. When the receiver was appointed just prior to the start of the profitable tourist season, on the first day he told me it did not matter how much of an assets surplus the company had, because I was personally liable for debts incurred while the business was insolvent and I would most likely end up losing my house. To date I am still unsure if this advice was correct. It would have been good to have been able ring an independent Government body like ASIC to get the correct advice on this matter. If I had been correctly informed I could have done things differently at the commencement of the receivership.

Over the past 10 years there has been an average of 11,300 insolvency appointments per annum, so the Insolvency Levy would provide funds of approx $15,000 per administration to enable a full time government employee to be assigned for up to 28 days to carry out an accurate investigation. Creditors could use this information to make informed decisions about the future of the company and appoint an administrator / liquidator or pass control back to the directors either with or without a DOCA.

Currently ASIC has approx 30 people dealing with 2% of complaints against insolvency practitioners and this well after the “horse has bolted”. This proposal would enable the number of people in this section to be increased to in excess of 1,000 and would provide a real assistance to the business community who would only have to recoup a very small percentage of their bad debts to make this proposal cash positive. It could also assist ASIC to locate rogue directors and educate creditors and directors about their rights and obligations under the Corporations Act. The $100 per annum levy costing $170 million per annum would represent less than 0.015 % of the economic activity of all companies in Australia and would be a very small cost for the potential benefits that could be gained.

Our company used to have less bad debts of than 0.5% of turnover per year (equivalent to $15,000 pa) and over half of these involved an insolvency practitioner where we received nothing and were given little or misleading information. We would have been happy to pay an extra $100 per annum to ensure we received accurate information about any company in difficulty as part of the initial administration process. The insolvency levy could be promoted as an aid to creditors getting some money rather than getting nothing from a corporate collapse, as happened for over 10 years with our company.

As an example the receivership of our company lasted for 19 months and cost well over $1 million including legal fees etc with the unsecured creditors receiving nothing. If ours was a normal situation for the 70% of insolvency appointments that are “profitable” for the insolvency practitioners, then by extrapolation this would have cost the economy about $8Bn over 19 months (approx $5Bn per annum) which was around 5% of GDP in 2005. Perhaps ours was not a normal receivership because our company had a substantial asset base?

I believe the insolvency levy would be of particular benefit to regional Australia and would prevent the premature destruction of vital infrastructure that is often difficult and costly to replace.

Definition for Acts of Good Faith to be added to the Corporations Law:

To also avoid confusion I recommend a definition for Acts of Good Faith be added to the insolvency sections in the Corporations to include but not be limited to:

1. Ensuring the true financial position of the company is accurately reported to creditors and ASIC
2. Collecting or making all attempts reasonably possible to collect all outstanding debtors in a timely manner so as to enable the business (if profitable) to continue to trade
3. Visiting major customers / tenants to discuss any pricing changes required in order to save the company and /or its business
4. Trying to sell the company and / or its business as a going concern rather than closing them down and sacking all of the employees
5. Providing payout figures which include all moneys collected and do not take into account possible future earnings or debtors owing to the administration
6. Making all attempts reasonably possible to continue the employment of pre-appointment employees of the business who are continuing to act in good faith and unless absolutely necessary not to replace these employees with personnel employed by the insolvency practitioners at significantly greater cost to the company
7. Employing managers or advisors who have substantial knowledge of the industry(s) in which the company and / or its business operates
8. In the case of a secured lender, first disposing of the assets over which it has prime security

If the insolvency practitioner does not do these acts then they would be seen to have not acted in Good Faith (similar to section 420A which deals with selling assets at not less than market value).

Risk Evaluation Method for Secured Lenders:

I recommend that a section be added to the legislation to require banks (secured lenders) and their appointed insolvency practitioners to evaluate the risks according to Australian Standard AS4360. In my case the bank appointed a receiver when it had no risk at all as it had first mortgage security on real estate worth over $2.9million to secure its loan of $1.8 million as well as a charge over 5 businesses turning over in excess of 3 million per annum and additional real estate worth $175,000.

Due to slow paying customers in the traditional non tourist season, our company had a cash flow problem which triggered one of 20+ “events of default” in the loan documentation, causing the bank to appoint receivers with their associated lawyers, agents, valuers etc who, over the following 19 months, charged well in excess of $1 million in fees and charges and, although the businesses were making a profit and no pre-appointment unsecured creditor was paid anything, somehow the bank ended up claiming a $358,000 shortfall at the conclusion of the receivership.

If the bank was required to evaluate its risks according to AS4360, this would have shown there was no risk to the bank at all and it should not have been able to appoint receivers, but rather let the administrator deal with the situation via the DOCA process to enable the business to continue to trade and employ 60 people as well as pay its unsecured creditors.

Receivers:

The Corporations Law needs to be changed so that secured creditors do not to take advantage of their position and appoint receivers who then take all the money and unsecured creditors get nothing. Has any company ever survived a receivership? It may well be best to abolish the receivership process altogether and let the mortgagee just sell the charged assets to recover their money. The only possible benefit to having a receiver is to trade out of the situation, but in the majority, if not all cases, this is not done. The use of the Administration process achieves the same outcome with the support of all the unsecured creditors.

There also needs to be a mechanism to prevent receivers from substantially under reporting receipts or over reporting liabilities to ASIC. Also the fees and charges of receivers should not be taken into account when determining the future profitability of the company they are controlling.

Liquidators:

A recent experience with a liquidator of a company that owes us about $25,000 has resulted in a similar outcome for unsecured creditors as the receivership of my company. Creditors have been left in the dark by the liquidator and will receive nothing. The liquidator was appointed in May 2009 and held the first and only meeting of creditors in January 2010 after he had incurred fees and charges in excess of $60,000, claiming the situation was very complicated and the requirements of ASIC caused him to do a considerable amount of work.

When I asked at the meeting for some very basic financial information about the company in liquidation (as there appears to have been fraud by the Director) the liquidator could not provide any financial information at all, but promised creditors he would produce a report within 1 month. I chased the Liquidator up after 2 months and received a short email claiming he had obtained legal advice that prevented him from disclosing any financial information to creditors and if I had any concerns to take them to the police. This is not possible for me without access to the figures.

Better Reporting and Complaint procedures for ASIC:

Both receivers and liquidators claim their high fees are as a result of the Corporations Law and they are only charging their scheduled rates. We need a more efficient process and the current process is un-Australian in that it does not appear to help the underdog at all.

I suggest Form 524 (Report As to Affairs) be modified to make insolvency practitioners report to ASIC the asset surplus / deficiency of a company excluding their fees and to make the legislation so as the practitioner cannot claim they are merely expressing an opinion.

Both liquidators and receivers appear to be accountable only to the Court and the way the legislation is currently written can only have their actions challenged in Court by ASIC, who appears only too happy to fob off that the matter as a civil dispute in the majority of cases. There needs to be a mechanism to enable a criminal complaint to be lodged with the court by the complainant if ASIC chooses not to take any action.

What we need for transparency is when a complaint is lodged, for ASIC not to just write their standard letter saying they have looked into the matter and have decided not to take any further action in this

case, and they will not challenge a matter of commercial judgment. They need to write back to the complainant and give details of the reply from the insolvency practitioner. If the complainant is not satisfied, perhaps a facilitated meeting between the parties would assist in resolving the matter – not ASIC just stating you can start your own civil proceedings if you want to.

If the insolvency practitioner lies to ASIC or gives "appropriate" answers to mislead ASIC, then ASIC personnel will not know unless the reply is challenged and the only person who would know if the answers are incorrect is the complainant, not ASIC. In a recent civil Court Case, the Barrister representing the other party cleverly mislead the Judge, who took what the Barrister said as being correct, until I challenged it. When I presented additional evidence to back up my claims, the Barrister's argument was defeated.

In my case most of the damage done to my company could have been avoided if ASIC had acted appropriately on my first complaint rather than sending me their standard letter. In my subsequent complaints ASIC seemed more interested in justifying their original decision not to take any action, rather than investigating the complaint and the additional information I provided. They never gave me any adequate reasons why they would not investigate the matters raised, only that they had decided not to take any action in this case and that they did not have to investigate every complaint.

Actions by the Australian Taxation Office:

I believe legislation or the guidelines should be enacted to prevent the collections section of the Australian Taxation Office from being able to pursue Directors of companies under external Administration until at least the Directors are able resume control of their company again.

In my case the ATO commenced bankruptcy proceedings against me under a Director Penalty Notice about 1 month after the unsecured creditors voted in favor of a DOCA. Because the bank had also appointed a receiver who told me "he held all the trump cards in this situation because the bank held a fixed and floating charge over the company", he was in charge of the realisation of approx $4 million of assets to repay the $1.6 million then owed to the bank. Because I was not in control of those assets I had no way of paying the ATO from the company. The personal bankruptcy proceedings were very stressful and effectively prevented from me from obtaining alternate finance to payout the bank and have the receivers removed. I was eventually able to prevent personal bankruptcy by selling a personal property and paying the ATO.

This is a very similar situation to Mr Andrew Garrett in Submission Number 13 who had the same firm of receivers as did my company, but ended up being bankrupted by the ATO because the receivers and the bank claimed the payout figure for the loan of $6million was over $10 million and when it appears his company had over $50 million in assets to be realised. Being bankrupted has effectively prevented Mr Garrett from taking effective action in the Courts to recover his losses.

Yours Faithfully,

Ron Coomer - Director