



31 January 2018

Senator the Hon Ian Macdonald
Chair
Senate Legal and Constitutional Affairs Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

By email: legcon.sen@aph.gov.au

Dear Senator

Bankruptcy Amendment (Enterprise Incentives) Bill 2017

Thank you for the opportunity for the Law Council to provide this submission to the Senate Legal and Constitutional Affairs Legislation Committee regarding the Bankruptcy Amendment (Enterprise Incentives) Bill 2017 (**the Bill**).

The Law Council acknowledges the assistance of its Insolvency and Reconstruction Committee of the Business Law Section (**the IRC**) and the Law Society of New South Wales (**the Law Society**) in the preparation of this submission.

The Law Council's focus on the specific provisions of the Bill is to ensure that the proposed changes do not unduly burden practitioners administering the process.

Background

The Bill seeks to implement changes announced on 7 December 2015 as part of the National Innovation and Science Agenda. Public consultation followed the issuing of Treasury Discussion Paper 'National Innovation and Science Agenda – Improving bankruptcy and insolvency laws' dated 29 April 2016 (**Discussion Paper**).

The Business Law Section made a previous submission to Treasury dated 26 May 2016 which touched on matters including the proposed changes to bankruptcy law set out in the Discussion Paper, a copy of which is enclosed.

Default period of bankruptcy

A reduction in the default period of bankruptcy from three years to one year was initially canvassed as one of the reforms proposed in the Discussion Paper. The Discussion Paper stated that the aim of the reforms was to drive a 'cultural shift' from penalising and stigmatising failure to encouraging entrepreneurship. The Law Council supports that aim.

The Bill does not distinguish between business and non-business bankruptcies. In its previous submission to the Treasury, the Business Law Section of the Law Council recommended that the reduction in the period of bankruptcy be restricted to business-related bankruptcy and should not apply to the majority of personal bankruptcies, which are consumer bankruptcies.

As the objective of the change in duration of bankruptcy is to encourage innovation and entrepreneurship the Law Council recommends that discharge from bankruptcy after one year should only be available as a possibility in bankruptcies that directly or substantially result from the failure of a business that commenced within the previous five years of the date of bankruptcy. This is a reasonable period to allow a business to test its viability.

The Law Society does not support the proposed general reduction in the default bankruptcy period. It has noted that the majority of personal bankruptcies are consumer, rather than business related. Further, it is questionable as to how the proposed measure can achieve its stated aim of encouraging innovation and business startups if the entrepreneurs targeted are not, at the present time, part of the demographic of individuals entering bankruptcy. The Law Society, however, supports the Law Council's recommendation for the measure to be targeted to business related bankruptcy.

Bankruptcy trustee

Where a bankrupt is seeking early discharge, the Law Council submits that the bankrupt should be required to provide evidence to the trustee to confirm that their bankruptcy is a business-related bankruptcy. The trustee would then be required to decide whether to approve the early discharge of the bankrupt and the duration of time prior to discharge. This decision would be subject to review by the Inspector General in Bankruptcy (**Inspector General**) in line with the current framework relating to objections to discharge. Following the Inspector General's determination, the decision could be appealed to the Administrative Appeals Tribunal or the Federal Court, depending on the nature of the grounds of review.

The Law Council suggests that the trustee's criteria should include a requirement to ensure that satisfactory arrangements exist to satisfy the bankrupt's obligations to make compulsory income contribution for the following two years. Further, it is possible that the express powers of a trustee could include the capacity to require a security bond to assist in enforcing compliance with post-bankruptcy obligations. This security bond would be automatically released to the estate for distribution if there are outstanding obligations following service of the requirements on the discharged bankrupt. However, the requirement for, and size of, the bond may be subject to review by the Inspector General.

Treatment of after acquired property

Assuming there was a distinction between business and other bankruptcies the issue of after acquired property (in particular unexpected winnings or inheritances) arises as it would be inequitable for a business bankrupt to retain such property where a non-business bankrupt (with a shorter bankruptcy) would not retain such property. The Law Council suggests that the Bill include a carve out provision to allow the realization of such

¹ Approximately 24% of bankruptcies in the June 2017 and September 2017 quarters were business related: Australian Government, *Statistics* (24 January 2018) Australian Financial Security Authority < <https://www.afsa.gov.au/about-us/statistics>>.

property from former business bankrupts in the relevant period of up to two years after discharge if a distinction between business and non-business bankruptcies was in place.

Introduction of a “registered address”

The obligations of a bankrupt should be extended to include a requirement to notify the trustee of, upon becoming bankrupt, an address within Australia at which their trustee may serve notices upon the bankrupt by prepaid mail or delivery (a ‘registered address’). Where appropriate, the obligations of the bankrupt should include informing the trustee of a change in their registered address. A requirement to have a registered address will shift the responsibility regarding which notices and proceedings have been served on the bankrupt from the trustee. As such, a bankrupt will be at risk if they do not, at all relevant times,² know what has been received at their registered address.

Section 149F and other sections of the *Bankruptcy Act 1966* (Cth) allowing a trustee to give notices requiring a bankrupt to take certain steps within the contribution of the assessment period,³ should be amended to allow service at the registered address. This amendment addresses the problems involved in contacting bankrupts given their capacity to travel overseas once discharged after one year without the trustee’s approval despite owing ongoing obligations to the trustee.

The Law Council suggests that amendments should be introduced to allow a trustee to serve proceedings issued pursuant to section 139ZG(3) of the *Bankruptcy Act 1966* (Cth), and any other relevant recovery proceedings, at the bankrupt’s registered address by mail or delivery.

Items 1 and 2 - Proposed amendments to section 59 of the Bankruptcy Act 1966 (Cth) (Act)

The Law Council suggests, for the sake of clarity, that the proposed amendment at the end of proposed subsection 59(1) be prefaced with the words ‘Subject to subsection (7)’.

Item 4 – Proposed amendment to section 80(1) of the Act

The Law Council suggests that it may be appropriate to add:

‘(d) any email address regularly used by the bankrupt for electronic communication;’

This inclusion could form part of broader reforms designed to introduce default address reporting requirements for bankrupts within the contribution assessment period, with similar operation to facilitate service as included in section 109X of the *Corporations Act 2001* (Cth).

In addition, the Law Council notes that the change from requiring notification to the trustee of a change in contact details from ‘immediately’ to ‘within 10 business days’ in a manner determined or approved by the trustee provides for a greater level of certainty for a bankrupt needing to comply and may assist to minimise disputation in any criminal prosecutions.

² Including while overseas.

³ See ss 139T(9), 139V, 139ZI(1) and 139ZIC(1) *Bankruptcy Act 1966* (Cth) for instances of giving notices.

Item 6 – Proposed amendment to section 139J (a) of the Act

The Law Council suggests, for the sake of clarity, that the words ‘during a period’ be replaced with the words ‘during the *contribution assessment period* under this division’.

Item 19 – Proposed amendment to section 149 of the Act

The Law Council reiterates that while it supports reducing the default period of bankruptcy the measure be targeted to business-related bankruptcy and not to the vast majority of personal bankruptcies being consumer bankruptcies.

The Law Society reiterates that it does not support the general reduction of the default bankruptcy period.

Items 23 - At the end of section 265 and Items 24-29- Section 277A

The Law Council supports these amendments and suggest consideration be given to providing for a similarly defined ‘prescribed period’ to apply in relation to the bankrupt’s obligations under section 77 of the Act.

Safeguards

If the above recommendations are not supported, the Law Council submits that certain safeguards described in the previous submission of the Business Law Section of the Law Council are not addressed in the Bill and should be considered. Firstly, credit reporting as to bankruptcy should be extended to cover the contribution assessment period (now to be defined in section 139K). Secondly, that disqualification from being a director of a company should be extended within the two year period following early discharge in circumstances where a bankrupt’s obligations to comply with notices served by their trustee are outstanding.

I trust these observations are of assistance.

Please contact Natasha Molt, Deputy Director of Policy
in the first instance, if you require further information or
clarification.

Yours sincerely

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Chief Executive Officer