27 October 2010

Mr Hamish Hansford
Committee Secretary
Senate Legal and Constitutional Committee
By email: legcon.sen@aph.gov.au

Dear Mr Hansford

Corporations Amendment (Sons of Gwalia) Bill 2010

We note that the Committee invites submissions on this Bill. The Insolvency Practitioners Association (IPA) appreciates this opportunity and provides the following comments, mainly on the drafting of the provisions. The IPA is the peak professional body representing company liquidators and trustees in bankruptcy, and lawyers, financiers academics and others practising in or otherwise interested in insolvency law and practice.

Drafting issues

Proposed section 563A says in effect that:

- the payment of a claim for a debt owed by the company to a person in the person's capacity as a member of the company (...) made against a company is to be postponed until all other claims made against the company are satisfied.

- the payment of any other claim that arises from a person buying, holding, selling or otherwise dealing in shares in the company made against a company is to be postponed until all other claims made against the company are satisfied.

This wording does not accord with section 553 of the *Corporations Act* which refers to "debts payable" (not owed) by the company, and to "all claims against" the company.

Further, proposed s 563A adds the word "made" - is that word "made" meant to add anything? While that may appear pedantic, sections such as 553 and others that seek to determine which creditors may or may not prove in an insolvency are interpreted closely by the courts.

We also contrast that with the wording of section 563B(2), that " ... payment of the interest is to be postponed until all other *debts and claims* in the winding up have been satisfied" rather than just *claims* in the proposed section 563A.

If there is a judgment debt obtained against the company by a person arising from the person buying, holding, selling or otherwise dealing in shares in the company, that debt may not be subordinated: see proposed section 563A(2)(b). This is because a debt is different from a mere claim. In that case, the shareholder who was misled, and who has

a judgment for the loss suffered, would be able to prove in the insolvency of the company along with all other creditors. That may be the appropriate policy. If it were not considered appropriate, the law should prevent that shareholder creditor from being able to prove in the insolvency despite having a judgment debt in its favour.

The question would then arise if that shareholder creditor has recovered its judgment debt from the company before its formal insolvency – should that creditor then be entitled to retain it, or should the law provide that the insolvency practitioner has a right of recovery of the amount paid to the shareholder by the company?

The proposed provisions do not directly deal with these issues and they are left unclear. In any event, such factual issues may arise and they will have to be dealt with under existing recovery provisions – for example those that allow the recovery of preferences paid to creditors – in the law.

We also consider that proposed section 563A will not prevent members from lodging proofs of debt, and therefore imposing an obligation on the practitioner under Corporations Regulation 5.6.52 to adjudicate and rule on those proofs. Some changes to the regulations may need to be made so that, for example, a practitioner is not required to deal with those proofs until such time that a dividend is to be paid in respect of subordinated claims.

Section 600H refers to a "person whose claim against a company is postponed" – strictly, what is postponed is the payment, not the claim.

We assume that the proposed section 600H should be included in the sections allowing electronic communications listed in section 600G of the *Corporations Act*?

Section 600H(b) allows a person to in effect apply to the court for the right to vote in the administration. We suggest the law should allow representative applications to the court on behalf of groups of shareholders, rather than requiring each individual shareholder to apply.

As to the application provision, it says that new s 563A, and s 600H, "applies to a claim that arises after this Schedule commences". The wording used in s 553 refers to a claim "the circumstances giving rise to which occurred before ..." etc. We consider section 553 adopts clearer wording which should be used in the application provision.

We have also read the revised submission of the Law Council of Australia of 20 October 2010. The IPA generally agrees with its comments on the drafting issues raised.

IPA support for the Bill

Finally, we emphasise that the IPA agrees with the overall purpose of this Bill to 'reverse' the High Court's decision in Sons of Gwalia. We have previously made submissions to government explaining the negative impact of that decision on insolvency administrations.

For the Committee's information, the recent decision of the Federal Court in *ION Limited, in the matter of ION Limited (Subject to Deed of Company Arrangement)* [2010] FCA 1119 illustrates the difficulties for a liquidator in managing large shareholder claims based on a company's alleged misrepresentations, and the need for the courts to intervene using existing law in order to facilitate the progress of those administrations.

We trust these comments are of assistance. Please contact Ms Kim Arnold, the IPA's Technical Director, on if you or the Committee wishes to discuss any aspect of our submission.

Yours sincerely

Michael Murray
Legal Director