Submission to the Parliamentary Joint Committee on Corporations and Financial Services

Australian Parliament House, Canberra

8 September 2022

Introduction[1]

1. The Committee has duties including inquiring into, and reporting on:

   1.1. the activities of ASIC and the Takeovers Panel, and matters connected with such activities; and

   1.2. the operation of the *Corporations Act* and the *ASIC Act* (as well as any Australian or foreign law that appears to affect significantly the operation of those Acts). [2]

2. This submission seeks to assist the Committee perform those duties by:

   2.1. providing a simplified outline and history of the *Corporations Act 2001* (Cth) (***Corporations Act***) and *Australian Securities and Investments Commission Act 2001* (Cth) (***ASIC Act***);

   2.2. identifying current issues for reform; and

   2.3. offering views of the Society of Corporate Law Academics' (the **Society**) on the Committee's work.

Simplified outline and history of the *Corporations Act* and *ASIC Act*

Corporations Act

3. The Commonwealth Parliament has limited power to make laws relating to corporations under the *Australian Constitution*. Before the 21st century, different legislation in each State and Territory created challenges for government and business across Australia. In the early 21st century, each of the States and Territories agreed to refer their legislative powers to the Commonwealth, allowing the federal *Corporations Act* to come into force, creating a consistent legislative regime for all of Australia.[3]

4. The *Corporations Act* is the principal legislation for Australian corporations, although corporations law encompasses other legislation, delegated legislation, common law, equity, and administrative guides.

5. Since its enactment, the *Corporations Act* has expanded significantly in scope and complexity. Presently, the *Corporations Act* provides:

   5.1. for the 'possible stages in the life of a company'[4] including its creation; normal operation; and abnormal operation, winding up, and dissolution;

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[1] This submission has been prepared by the following members of the Society of Corporate Law Academics and its Executive: Emeritus Professor Stephen Bottomley FAAL (ANU), Associate Professor Vivienne Brand (Flinders), Associate Professor Michael Duffy (Monash), Associate Professor Anil Hargovan (UNSW), Associate Professor Marina Nehme (UNSW), Associate Professor Beth Nosworthy (Adelaide) and Dr Michelle Worthington (ANU). Further information on each member is provided in the Appendix. The Society also acknowledges the assistance provided by Jordan Tutton in preparing this submission.

[2] *Australian Securities and Investments Commission Act 2001* (Cth) s 243.

[3] Robert Austin and Ian Ramsay, LexisNexis Butterworths, *Principles of Corporations Law* (online at 27 August 2022) [2.310]; Australian Law Reform Commission, *Historical Legislative Developments* (Background Paper FSL4, November 2021); *Corporations Act 2001* (Cth) s 3; see, eg, *Corporations (Commonwealth Powers) Proclamation 2021* (NSW).

[4] Austin and Ramsay (n 3) [1.030].

5.2. for powers, duties and rights of individuals involved with companies, such as directors, managers, promoters, members, auditors and others;

5.3. specific regulation relating to financial services and markets;[5]

5.4. ASIC with regulatory functions and powers to administer and enforce the Act; and

5.5. the courts with jurisdiction and powers with respect to civil and criminal proceedings.

ASIC Act

6. ASIC is the national 'corporate, markets, financial services and consumer credit regulator.'[6] The *ASIC Act* establishes ASIC, the Takeovers Panel, and this Committee (among other things). In brief:

 6.1. Part 2, Division 2 relates to unconscionable conduct and consumer protection in respect of financial services. The operation of these provisions are not directly included in the Committee's remit;[7]

 6.2. Parts 3, 3A and 3B provides ASIC with information gathering powers, investigation processes, and other regulatory tools;

 6.3. Parts 4, 5, 6, 7 and 8 relate to ASIC's business, staff and reporting requirements;

 6.4. Parts 9, 10 and 11 relate to financial services and credit panels, the Takeovers Panel and the Companies Auditors Disciplinary Board (respectively); and

 6.5. Part 12 relates to the Australian financial reporting system, in particular the accounting, auditing and assurance standards to be applied in Australia.

7. In addition to ASIC's responsibilities under the *Corporations Act* and *ASIC Act*, it has functions and powers arising under insurance, superannuation and consumer credit laws.[8]

8. Overall, ASIC is intended to (among other things):

 8.1. maintain, facilitate and improve the performance of the financial system and entities within it in the interests of commercial certainty, reducing business costs, and the efficiency and development of the economy;

 8.2. promote confident and informed participation in the financial system;

 8.3. administer the law effectively and with minimal procedural requirements; and

 8.4. take whatever action it can, and which is necessary, to enforce and give effect to the law.[9]

9. ASIC seeks to achieve these outcomes through its activities in:

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[5] See *Corporations Act 2001* (Cth) ch 7.

[6] ASIC, *Annual Report 2020–2021* (October 2021) 9.

[7] *Australian Securities and Investments Commission Act 2001* (Cth) s 243(a)(ii); see also s 5 (definition of 'excluded provisions').

[8] See *Australian Securities and Investments Commission Act 2001* (Cth) s 12A(1). These include the *Banking Act 1959* (Cth); *Business Names Registration Act 2011* (Cth); *Insurance Contracts Act 1984* (Cth); *National Consumer Credit Protection Act 2009* (Cth); and *Superannuation Industry (Supervision) Act 1993* (Cth).

[9] ASIC, *Annual Report 2020–2021* (October 2021) 9; *ASIC Act* s 1(2).

9.1. institutional and governance supervision;

9.2. surveillance;

9.3. enforcement (such as investigations, criminal proceedings, civil proceedings, and administrative actions);

9.4. determining applications for relief from the *Corporations Act*;

9.5. licensing and professional registration (such as for Australian Financial Services Licences, credit licences, liquidator registrations, and auditor registrations);

9.6. consultation with, and guidance to, industry; and

9.7. consumer education.[10]

10. Importantly, under Australia's 'twin peaks' model of financial regulation, responsibility for regulating market conduct is assigned to ASIC, while prudential regulation is the responsibility of a separate regulator (APRA).[11]

11. The Committee has recently reviewed ASIC's governance arrangements, following some concerns arising out of events surrounding ASIC's 'handling of two questionable decisions related to the remuneration of its then Chair and one of its then Deputy Chairs'.[12]

Current issues for reform

12. In this section, the Society highlights five current issues for reform, and notes several additional issues that are the subject of existing reform activities. The five issues, and the presenters for those issues, are:

12.1. *Re-establishing the Corporations and Market Advisory Committee:* Presenter – Emeritus Professor Stephen Bottomley;

12.2. *Corporate structures – Proprietary and public companies*: Presenter – Associate Professor Marina Nehme;

12.3. *Corporate structures – Categorisation and social purpose:* Presenter – Associate Professor Beth Nosworthy;

12.4. *Fault elements in securities non-disclosure liability:* Presenter – Associate Professor Michael Duffy;

12.5. *Insolvency law – Root and branch review*: Presenter – Associate Professor Anil Hargovan.

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[10] See ASIC, *Annual Report 2020–2021* (October 2021) 31–36, 68.

[11] Andrew Godwin, Ian Ramsay and Andrew Schmulow, 'Twin Peaks in Australia: The Never-Ending Trek?' in Andrew Godwin and Andrew Schmulow (eds), *The Cambridge Handbook of Twin Peaks Financial Regulation* (Cambridge University Press, 2021) 71.

[12] Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Oversight of ASIC, the Takeovers Panel and the Corporations Legislation No 1 of the 46th Parliament* (Report, March 2022) [2.1].

Issue 1: Re-establishing the Corporations and Market Advisory Committee[13]

13. The Society strongly recommends the re-establishment of the Corporations and Markets Advisory Committee (**CAMAC**), or the creation of a similar body, to allow for the provision of independent, expert advice to government in the areas of corporate law and governance, the regulation of financial markets and insolvency (collectively referred to as 'corporations law').

14. **Background**: CAMAC was originally established as the Companies and Securities Advisory Committee (**CASAC**) in September 1989,[14] but was renamed to CAMAC in March 2002.[15] However, in its original guise, it replaced the Companies and Securities Law Review Committee, which was first established in 1983.[16]

15. CAMAC's functions were set out in section 148(1) of the *ASIC Act*, which provided:

> CAMAC's functions are, on its own initiative or when requested by the Minister, to advise the Minister, and to make to the Minister such recommendations as it thinks fit, about any matter connected with:
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> (a) a proposal to make corporations legislation, or to make amendments of the corporations legislation; or
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> (b) the operation or administration of the corporations legislation; or
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> (c) law reform in relation to the corporations legislation; or
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> (d) companies or a segment of the financial products and financial services industry; or
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> (e) a proposal for improving the efficiency of the financial markets.[17]

16. In executing its functions, CAMAC's ordinary course was to develop and publish a consultation paper on certain nominated issues, and to call for submissions from the public in relation to that consultation paper.[18] After due consideration of submissions, CAMAC would produce a final report, which it would then provide to the responsible Minister.[19] CAMAC was designed to ensure that business interests, as well as those of the various state and territory governments were properly accounted for in corporations law reform discussions, with section 147 specifying that such interests were to be reflected in CAMAC's membership.

17. CAMAC's ability to act 'on its own initiative' was one of its many strengths as an expert advisory body; this capacity helped to ensure that CAMAC was not only able to respond to developments in the field of corporations law, but that it could also *anticipate* important developments. In a field as dynamic as corporations law such capacity was welcome, and CAMAC and its immediate predecessor exercised this capacity on a number of occasions.[20]

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[13] This sub-section has been provided by Dr Michelle Worthington.

[14] Ian Ramsay, 'A History of the Corporations and Markets Advisory Committee and its Predecessors' in Pamela Hanrahan and Justice Ashley Black (eds), *Contemporary Issues in Corporate and Competition Law: Essays in Honour of Professor Robert Baxt AO* (LexisNexis, 2019) 59, citing CASAC, *Annual Report 1991–1992* (1992), 1. The Society is grateful to Professor Ramsay for his having so meticulously documented CAMAC's history and operations.

[15] Ramsay (n 14) 60.

[16] Ibid 57, citing the CSLRC, *Annual Report for the period 1 January to 30 June 1984*, 2.

[17] For ease of reading, we have removed the text reading '(other than the excluded provisions)' from subsections (a), (b) and (c).

[18] Ramsay (n 14) 60.

[19] Ibid.

[20] Ibid, citing John Kluver 'Future Directions in Corporations and Securities Law' (1993) 3 *Australian Journal of Corporate Law* 230, 232, Table 1.

18. CAMAC was defunded in 2014,[21] and the legislative provisions providing for the establishment, functions and operations of CAMAC were eventually repealed in 2018.[22] This followed a recommendation from the National Commission of Audit in 2014 that CAMAC be consolidated into the Department of Treasury.[23] As Professor Ian Ramsay has noted the only explanation for the flagged abolition of CAMAC was a brief note in the 2014–2015 budget papers which provided 'the Government will achieve savings of $19.4 million over four years from 2014–2015 by abolishing some government bodies and merging other government bodies to reduce duplication, improve coordination and increase efficiency in how public funds are used to deliver services to the community'.[24] An almost identical, equally brief explanation was given for the eventual repeal of the relevant legislative provisions in 2018.[25]

19. The abolition of CAMAC was an unanticipated and controversial development, and was widely opposed by leading professional, industry and legal experts.[26] The vast majority of submissions received in response to the Senate Economics Legislation Committee Inquiry into the proposed abolition of CAMAC, advocated for the retention of CAMAC; in fact, only a single submission spoke in favour of the proposed abolition.[27]

20. The Society considers that CAMAC's work was extraordinarily valuable, not least by virtue of its impact on corporations law reform, the depth and scope of the expertise underpinning the work of CAMAC, its independence as an advisory body, its ability to enhance consultation processes in relation to corporations law reform, and finally, its remarkable cost effectiveness.

21. **Impactful**: CAMAC and its predecessors were both active and effective, providing a steady stream of the highest calibre advice to successive governments for over three decades. Between 1984 and 2014 CAMAC and its predecessors produced **54 reports** on a wide range of corporations law issues.[28] As discussed in the then Corporate Law Teachers Association submission in response to the exposure draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014, CAMAC and its predecessors have actively shaped law reform in Australia, an influence that is discussed in the various explanatory memoranda accompanying important legislative reforms.[29] It is not possible to set out the full scope of that influence here, however to illustrate the extent to which important reforms have drawn on the work of CAMAC and its predecessors, we note the explanatory memorandum accompanying the Howard Government's Corporations Amendment (Insolvency) Bill 2007 mentions CAMAC's work no less than 42 times.[30] Recommendations from CAMAC and its predecessors were implemented by successive governments in relation to a range of matters

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[21] Ramsay (n 14) 68.

[22] Ibid.

[23] Ramsay (n 14) 61, citing National Commission of Audit, *Towards Responsible Government: Phase One* (February 2014) 216.

[24] Ramsay (n 14) 61, quoting Commonwealth Budget Papers, *Budget Paper No 2, Budget Measures 2014–2015*, Expense Measures (2014) page 70.

[25] Ramsay (n 14) 68, quoting Explanatory Memorandum, Statute Update (Smaller Government) Bill 2017 (Cth) [78].

[26] Ramsay (n 14) 56, 63–66.

[27] The remaining 15 submissions were opposed to the proposed abolition: Ramsay (n 14) 63.

[28] See Ramsay (n 14) Appendices 1 and 2.

[29] Corporate Law Teachers Association, *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (29 October 2014) 2.

[30] Ibid.

including (but not limited to) takeovers, continuous disclosure, uncertified securities, shareholder voting and statutory derivative actions.[31]

22. **Depth and Scope of Expertise**: Corporations law is notorious for its complexity. The Society submits that an independent body dedicated to matters of corporations law reform is an essential ingredient for effective, informed corporations law reform. While statutory schemes play an important role in corporations law, it remains an area closely governed by the common law and equity (the law on directors' duties is a particularly good example of this). Part of the challenge involved in the design and implementation of corporations law reform is the complex interplay of statutory and general law principles and rules. Following the abolition of CAMAC, Australian parliaments and the Australian people have lost a vital source of expert advice on the common law and equity as it pertains to corporations and financial markets. This is due to the fact that Treasury's remit concerns only the relevant legislation; CAMAC's function, by contrast, was broader, allowing for the provision of more fulsomely contextualised advice to government on law reform proposals in and around corporations law. Reinstating CAMAC or equivalent body will plug what is a substantial gap in the Government's existing law reform framework. For example, a body such as CAMAC could of its own volition investigate and advise on critical ESG (Environmental, social and governance) issues such as the extent to which company directors are permitted or indeed required to respond to environmental and social risks in satisfying their directorial obligations, which arise under statute, the common law and equity. Company directors and officers sorely need guidance on these central and complex matters, but such guidance could only be provided by those with expertise in both statutory and general law matters, not to mention the management of companies and company groups.

23. **Independent Advice**: If it is to maintain its position as a leading corporate law jurisdiction, Australia's approach to corporate law reform must be guided by the best possible advice to government, including of course, advice that is independent of government. An independent and hence neutral statutory body such as CAMAC allows for more wholistic consideration of issues; within such a body the views and needs of government, industry and the professions can be blended together with comparative ease.

24. **Enhanced Consultation**: A related point is that an independent, expert body such as CAMAC allows for enhanced consultation on matters of corporations law reform, as consultation processes are by design 'in built'. For example, when CAMAC released a consultation paper as part of an inquiry, that consultation paper was one that already reflected a range of stakeholder perspectives, including industry, legal and consumer perspectives. This is due to CAMAC's unique composition, it being a body constituted by independent experts from a range of different backgrounds, including importantly, the various states and territories that comprise the federal compact.[32] It is for this reason perhaps unsurprising that the entities most vocally opposed to the abolition of CAMAC included peak industry and professional bodies such as the Governance Institute of Australia, The Australian Institute of Company Directors, Chartered Accountants Australia and New Zealand, CPA Australia,[33] the Australian Shareholders Association,[34] as well as the Law Societies of New

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[31] Ramsay (n 14) Appendix 3.

[32] See, eg, the now repealed section 147 of the *Australian Securities and Investments Commission Act 2001* (Cth).

[33] See, eg, Governance Institute of Australia, Australian Institute of Company Directors, Chartered Accountants Australia and New Zealand, CPA Australia, *Joint Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (24 October 2014) 1.

[34] See, eg, Australian Shareholders Association, *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (15 October 2014) 1.

South Wales,[35] Queensland[36] and Western Australia[37] and the Law Council of Australia.[38] The Society submits that an independent, expert body such as CAMAC is best placed to provide the highest possible degree of consultation with all relevant stakeholders in matters of corporate law reform on an ongoing and continuous basis, consultation which is essential to the successful development and maintenance of corporations law in Australia. We note that such enhanced consultation is critical to the success of law reform, including because it is likely to encourage 'buy-in' from those most likely to be affected by law reform proposals.

25. **Cost effective:** The Society submits that CAMAC and its predecessors operated in an extremely cost-effective way, delivering excellent value to the Australian taxpayer. At the time of its abolition, CAMAC's operating budget was 'modest',[39] totally less than $1 million per annum.[40] From 1991 to 2014, over 150 experts contributed to the work of CAMAC and CASAC,[41] and overwhelmingly this work was done on a low cost or no cost basis.[42] CAMAC's remarkable productivity was achieved with only a small permanent staff (2 lawyers and 1 administrative assistant at the time of abolition).[43] The Society submits that that the costs of securing the same quality of advice from industry and legal experts outside a CAMAC like-structure are likely to far exceed those associated with the running of CAMAC over time.

Issue 2: Corporate structures – Proprietary and public companies[44]

26. While this year we have had the introduction of corporate collective investment vehicles as a new form of corporation, the basic structure of companies has not been the subject of a rethink despite a range of commentaries criticising the existing structures and lobbying for the creation of new structures such as community benefit corporations.

27. In term of structure, companies may be classified as proprietary company or public company. Proprietary companies are private entities who, in principle, should not have more than 50 non-employee shareholders. Furthermore, due to its private nature, the company is not able to raise capital from the market through the issue of securities (section 113 of the *Corporations Act*). Public companies on the other hand are companies that may have unlimited number of shareholders and may issue securities to the public as long as they comply with the disclosure requirements set up

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[35] See, eg, Law Society of New South Wales, *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (23 October 2014) 1.

[36] Se, eg, Queensland Law Society, *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (24 October 2014) 1.

[37] See, eg, Law Society of Western Australia, *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (24 October 2014) 11.

[38] See, eg, Law Council of Australia (Business Law Section), *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (22 October 2014) 1.

[39] Ibid 8.

[40] Australian Restructuring, Insolvency & Turnaround Association, *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (9 October 2014) 1.

[41] Ramsay (n 14) 69.

[42] Law Society of Western Australia (n 37) 8.

[43] Law Council of Australia (Business Law Section), *Submission on the Exposure Draft of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014* (22 October 2014) 3.

[44] This sub-section has been provided by Associate Professor Marina Nehme.

under Chapter 6D of the *Corporations Act*. Over 98% of companies registered with ASIC are proprietary companies.

28. This distinction between public and proprietary companies has been in place since the nineteenth century and in view of the recent amendments to corporate law and the changes in community's needs and expectations, it is time to revisit this distinction. One example that highlights this is that proprietary companies, when they meet certain requirements, are able to issue shares to the public through the use of crowd-sourced funding. In doing so, they will end up having a membership that goes beyond the maximum that was originally prescribed under the legislation. Additionally, members will have less protection than the ones provided for public companies. Accordingly, it is time to conduct a review to ensure that our corporations law remains fit for purpose.

Issue 3: Corporate structures – Categorisation and social purpose[45]

Recommendation

29. The Society recommends that the Committee review the existing framework within the *Corporations Act* to:

    29.1. provide consistency across the law in what is considered 'small';

    29.2. re-examine duties owed by officers and directors within companies of various sizes; and

    29.3. enact a specific corporate form for social or public purpose companies

Background

30. Currently, as noted above, the existing framework of the *Corporations Act* permits incorporation as either a proprietary or a public company. Within the proprietary company form, there is a further sub-division into small and large proprietary company, with the distinction being made according to size limits initially established in section 45A of the *Corporations Act*.

31. The *Corporations Amendment (Proprietary Company Thresholds) Regulations 2019* doubled the limits contained in that section. Although the original values in the *Corporations Act* undoubtedly required reconsideration, the current location of the new 'large' threshold in the Regulations is less than ideal. Further, it is challenging to understand a company with annual consolidated revenue of up to $50 million, gross assets of up to $25 million and up to 100 employees as 'small'. These limits are not applied consistently in our laws, with different thresholds applied in tax, for example, as will be discussed below in relation to Insolvency Reform (see below at [66] and following). Reform would be welcome to ensure consistency of categorisation across all laws.

32. Further, dependent on considerations raised above, it must be asked whether it is still appropriate to regulate single director/shareholder companies in the same way as public companies of significant size and scale, or even to regulate all entities within the one legislative instrument.

33. As a general rule, the duties of directors and officers are owed to the company entity, and not to individuals, such as shareholders. That is not necessarily to recommend higher regulation for larger companies – indeed, it may be possible for a sole director of a small proprietary company to do more harm, albeit on a more limited scale, due to their ability to act on their own. With limited exceptions, for example disclosure and voting in public companies for directors with a material personal interest,[46] the duties of directors and officers remain consistent across companies of all shapes and sizes. There is value in the certainty this legislative unity provides, but the general law

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[45] This sub-section has been provided by Associate Professor Beth Nosworthy.

[46] *Corporations Act 2001* (Cth) s 195.

recognises variations in the duties owed by those in authority, particularly for closely-held companies,[47] and particularly where the 'relationships [between directors and shareholders] are not impersonal but close'.[48]

34. This is no small matter. According to the Australian Bureau of Statistics, as of 2021, of the 2.4 million operating businesses in Australia, nearly one million used a company structure.[49] Of those operating businesses, 93% had a turnover of less than $2m, and 97.1% employed less than 20 staff in total (58.3% were non-employing, and a further 38.8% employed between one and 19 staff).[50] Individually their contributions to our economy may be small, but they are vast in number – far outweighing the large corporate entities which dominate advertising and news cycles. This significant percentage of our business community is collectively labelled 'small', according to the *Corporations Act*, but provided with no further specialist regulation beyond relief from the requirement to undertake annual general meetings, compile directors' reports and annual financial reports, or appoint an auditor for those reports.[51]

35. A further area for reform is the introduction of a corporate vehicle designed for social purpose or social enterprise. Under an orthodox approach to the law, Australia (along with most other common law countries, and indeed a number of civil law countries) is understood to be a 'shareholder primacy' jurisdiction.[52] According to this theory, in such jurisdictions, the primary focus of directors and the company in decision-making should be on the shareholders, and particularly on maximisation of shareholder value. It is, undoubtedly, more nuanced than this – and has been throughout discussion of these principles for the past 100 years.[53]

36. This position is countered by those who advocate for a 'stakeholder focus', which emphasises the need for decision-making to take into account the diverse interests of key stakeholders for the business, which could be as wide-ranging as shareholders, employees, local community and the environment in which the business operates.[54] These theories underpin a movement in recent

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[47] See, eg, *Brunninghausen v Glavanics* (1999) 46 NSWLR 538, following *Coleman v Myers* [1977] 2 NZLR 225. Similarly in the UK: *Re Chez Nico (Restaurants) Ltd* [1992] BCLC 192; *Platt v Platt* [1999] 2 BCLC 745.

[48] *Glavanics v Brunninghausen* (1996) 19 ACSR 204, 217.

[49] Australian Bureau of Statistics, *Counts of Australian Businesses including Entries and Exits, from July 2017–June 2021* (24 August 2021).

[50] As above.

[51] Small proprietary companies are not subject to a number of provisions of the *Corporations Act 2001* (Cth), including ss 292(1), 298, 327A, but may elect to comply with them, be required to by their constitution, or may be requested to comply by ASIC.

[52] See, eg, Tim Connor and Andrew O'Beid, 'Clarifying Terms in the Debate Regarding "Shareholder Primacy"' (2020) 35(3) *Australian Journal of Corporate Law* 276; Jean J du Plessis, 'Directors' Duty to Act in the Best Interests of the Corporation: "Hard Cases Make Bad Law"' (2019) 34(1) *Australian Journal of Corporate Law* 3; Pamela Hanrahan, 'Companies, Corporate Officers and Public Interests: Are We at a Legal Tipping Point?' (2019) 36(8) *Company and Securities Law Journal* 665; Jason Harris, 'Revisiting the Legal Basis of Shareholder Primacy' (2019) 71(2) *Governance Directions* 76.

[53] Arguably, much of this discussion commenced with a series of papers in the *Harvard Law Review* between Professors Berle and Dodd: AA Berle Jr, 'Corporate Powers as Powers in Trust' (1931) 44 *Harvard Law Review* 1049 and E Merrick Dodd Jr, 'For Whom Are Corporate Managers Trustees?' (1932) 45 *Harvard Law Review* 1145.

[54] For further discussion, see, eg, Manuel Castelo Branco and Lúcia Lima Rodrigues, 'Positioning Stakeholder Theory within the Debate on Corporate Social Responsibility' (2007) 12(1) *Electronic Journal of Business Ethics and Organization Studies* 5; Susan Glazebrook, 'Meeting the Challenge of Corporate Governance in the 21st Century' (2019) 34(2) *Australian Journal of Corporate Law* 106; Henry Hansmaan and Reinier Kraakman, 'The End of History for Corporate Law' (2001) 89(2) *Georgetown Law Journal* 439; Andrew Keay, 'Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's "Enlightened Shareholder Value Approach"' (2007) 29(4) *Sydney Law Review* 577.

decades towards recognition of company structures which centre themselves explicitly on some broader public or social purpose, rather than solely on shareholder profit.

37. Internationally, there are a number of specific corporate structures available for businesses which operate with a social, environmental or other governance purpose. For example, in the United Kingdom, a company can register as a 'community interest company' (CIC) – a special type of limited company which operates explicitly to benefit the community, rather than shareholders.[55] Similarly, a variety of benefit corporation models are available in most jurisdictions within the US, know variously as low-profit limited liability companies (L3C), flexible purpose corporations, social purpose corporations, benefit corporations and benefit LLCs.[56] They can provide a middle-ground for a private enterprise to benefit alongside charities from a tax perspective, due to their social mission or public purpose – but they can also simply identify to consumers and investors that although this business is 'for profit', it also serves a 'mission to advance the common good'.[57]

38. Australia currently provides no such vehicle, beyond the public company limited by guarantee, which is subject to the same high level of oversight and regulation as other public company structures, and may not be appropriate for a small business particularly in its early years. Without a specific corporate structure for registration, companies are seeking private 'certification', provided by independent organisations such as B Lab,[58] to indicate to consumers that they are a for-profit enterprise with a social or environmental purpose.

39. Historically, Australia once required companies to set out their purposes in an 'objects' clause of their company constitution. However, in part because this could lead to questions of whether a company was acting 'beyond power' (or ultra vires), this is no longer mandated, with the exception of 'no liability' companies under section 112 of the *Corporations Act*. Companies can, voluntarily, include a purpose or objects clause in their constitution, and this constitutional addition underpins most private certification processes (such as B Lab). The risk inherent in resting on such an approach, without the provision of a specific corporate structure for such purpose corporations is that there is no clear indication to either internal parties - such as members, who may have access to the constitution but may not have read or engaged with it, or external parties such as creditors, who are far less likely to have access to that document – that the company is pursuing a specific purpose. Although there are protections available for third parties in the *Corporations Act* who have not read or engaged with the company constitution prior to contracting,[59] this post hoc protection is not preferable to a specific model of incorporation designed for these businesses.

40. Reform in this space would provide an opportunity to maintain the bright line between for-profit entities (subject to tax) and not for profit or charitable entities; provide clarity to investors as to the focus of the companies bottom line; and enable consumers to make an educated decision in their engagement with businesses claiming a social or public purpose. A key element of reform in this space would be consideration of whether non-shareholder stakeholders would have any standing to enforce social or public purposes espouses by such companies – under the current structure of the *Corporations Act*, the ability to bring such an action would be limited to members, affected officers or directors, or persons who have previously held such positions.[60]

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[55] As discussed by the UK Government: 'Setting up a social enterprise' (Web Page).

[56] Orrick, Herrington & Sutcliffe LLP, UnLtd and Thomson Reuters Foundation, *Balancing Purpose and Profit: Legal Mechanisms to Lock in Social Mission for 'Profit with Purpose' Businesses Across the G8* (Report, December 2014) 7.

[57] Ibid 4.

[58] See, eg, https://www.bcorporation.net/en-us/ a service which provides a fixed fee rate per year for a business to be labelled as a 'B Corp'.

[59] See, eg, *Corporations Act 2001* (Cth) ss 128–129.

[60] See, eg, *Corporations Act 2001* (Cth) ss 234, 236.

Issue 4: Fault elements in securities non-disclosure liability[61]

41. This submission focuses on the 2021 changes to continuous disclosure (sections 674(1) to 674A) and misleading and deceptive conduct (section 1041H) provisions in the *Corporations Act* and misleading and deceptive conduct (section 12DA) in the *ASIC Act* ('the changes') which introduce the requirement of showing fault elements of knowledge, recklessness or negligence of the corporation or its officers in order for liability to attach.

Continuous disclosure

42. The objective and/or effect of the changes appears to be that:

    42.1. the former continuous disclosure contravention remains as an offence but is no longer a civil penalty provision; while

    42.2. a new form of continuous disclosure contravention, involving knowledge, recklessness or negligence is enacted and is a financial services civil penalty provision (entailing a right to compensation under section 1317HA) but not an offence.

Misleading and deceptive conduct

43. The objective and/or effect of the changes to section 1041H and section 12DA appears to be to introduce the same fault elements where misleading or deceptive conduct claims are brought on the basis of the same conduct as continuous disclosure breaches.

Background

44. Securities disclosure laws are designed to ensure investors are given the most accurate information on companies that they invest in. Securities claims, including class actions, can seek to recover compensation when this does not occur and, in doing so, hopefully deter future such disclosure breaches.

45. After amendments to the law in 2021 knowledge, recklessness or negligence of corporations must be proven in such claims for investors to recover and/or for ASIC to obtain relief for breach of a civil penalty obligation (ASIC may still bring criminal action, which pursuant to the Criminal Code would appear to require either intention or recklessness[62] or may bring an infringement notice). Though the relevant laws are about civil penalty provisions, much of the debate has arisen due to the prevalence of private civil actions for damages (especially class actions) pursuant to the availability under section 1317HA of compensation for breach of civil penalty provisions (which compensation is available whether or not a declaration of contravention of the civil penalty provision has been made by a court).

46. The fault elements may be seen to be at least as significant to the position of corporations themselves as to officers given that the former are most often targeted in shareholder class actions[63] (with officers sometimes added as defendants). Corporations as defendants themselves (and sometimes insurers) appear to be significant funders of class action damages paid to plaintiffs.[64]

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[61] This sub-section has been provided by Associate Professor Michael Duffy.

[62] *Criminal Code Act 1995* (Cth) ss 5.6(1), (2).

[63] M Duffy, 'Australian private securities class actions and public interest - assessing the 'private attorney-general' by reference to the rationales of public enforcement' (2017) 32(2) *Australian Journal of Corporate Law* 162.

[64] M Duffy, 'Protection of Companies from Shareholder Class Actions Through Constitutional Amendment: Is This Possible or Desirable?' (2011) 23(1) *Bond Law Review* 1, 17.

The debate about the changes

47. There were essentially two competing policy views as to these changes which might be summarised as follows.

48. The view in favour of the changes was that, without requirements of proving fault:

    48.1. liability was 'strict' and attached too easily to corporations which then became a significant cost to shareholders and insurers in funding settlements to plaintiffs;

    48.2. it was too easy for plaintiff lawyers, funders and a group of current or former shareholders to obtain substantial sums[65] in 'opportunistic' class actions against listed corporations; and

    48.3. listed corporations were being penalised for unintentional and non-negligent behaviour.

49. The view against the changes was that that requirements of proof of fault:

    49.1. would make such shareholder claims substantially more difficult to prosecute, prove and obtain compensation;

    49.2. that this then would make it too easy for corporations to have lax or inadequate disclosure practices; and

    49.3. that this would reduce the rights of redress of investors who had invested substantial sums of money in listed corporations on the basis of what corporations said about themselves, (or failed to say about themselves).

Some options

50. The main policy options in this area appear to be as follows:

    Option One: Leave the changes intact and, as already required under the legislation,[66] require a review of their operation after a period of two years.

    Option Two: Repeal the changes and revert to the earlier position.

    Option Three: Investigate other options including:

    (b) Repeal the changes but at the same time investigate and then create a stronger 'safe harbour' defence or 'due diligence' defence for companies and officers that behave reasonably and honestly.

    (c) Leave the changes intact for now but at the same time investigate and then create a stronger 'safe harbour' defence or 'due diligence' defence for companies and officers that behave reasonably and honestly, following which the changes would be repealed.

[65] Mostly seven, eight or nine figure settlement sums in shareholder class actions. See Peter Cashman and Amelia Simpson, 'Costs and Funding Commissions in Class Actions', Supplementary Submission No 55.3 to Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into Litigation Funding and the Regulation of the Class Action Industry* (26 October 2020).

[66] *Corporations Act 2001* (Cth) s 1683C.

Discussion

51. Option Three would assist plaintiffs/ASIC in reducing the evidential onus on them. This would be averse to defendants but defendants would also benefit in the creation a new defence (but this would also impose on defendants the evidential onus of proving that defence).

52. It is noted that section 1317S of the *Corporations Act* already allows relief for a defendant from liability where a person (which would appear to include a corporation[67]) has acted honestly and ought fairly to be excused from liability. It has been suggested that though this section gives a wide discretion to courts to excuse company officers from liability where it would be unjust or oppressive not to do so, this provides 'relief' rather than a 'defence' as it does not prevent an initial finding of breach of the law.[68]

53. In discussions of whether the former legislative provisions were 'strict liability' and the meaning of this term, it is also useful to note that strict liability may not be the most severe or 'strict' form of application of a law, given that 'absolute liability' is suggested as the strictest form.[69]

Issue 5: Insolvency law – Root and branch review[70]

54. The submission focuses on the need for comprehensive insolvency law reform and advocates for the Committee to consider a 'root and branch' review,[71] akin to that undertaken by the Harmer Report nearly thirty-five years ago,[72] to assess whether Australia's insolvency and restructuring procedures are fit for purpose.[73]

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[67] This relies on interpreting a 'person' as including a corporation as s 2C of the *Acts Interpretation 1901* (Cth) does (see also Austin and Ramsay at [16.100]). This is not overly controversial as corporations are legal persons. There is no definition of 'person' in s 9 of the *Corporations Act* other than to say it includes a superannuation fund in ss 200 to 200J and in s761A to say it might be a partnership. Austin and Ramsay also footnote dicta in *Blue Metal Industries* [1970] AC 827; (1969) 117 CLR 651 that an Interpretation Act is a drafting convenience and would not be expected to be used to change the character of legislation. Note that s 1317G in prescribing penalties for 'persons' who breach civil penalties provides two different amounts – for 'an individual' and for a 'body corporate'.

[68] Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Litigation Funding and the Regulation of the Class Action Industry* (Report, December 2020) 326–327.

[69] Distinction set out in Bronitt and McSherry's *Principles of Criminal Law* at [3.230]. It may be then that gradations of liability might be set out from least 'strict' to most 'strict' as follows: (a) criminal fault elements required to be proved – evidential onus on Crown to prove fault through intention or recklessness required; (b) fault required to be proved including negligence option – evidential onus on plaintiff/ASIC to prove fault elements of knowledge, recklessness or negligence; (c) strict liability with a defence – fault elements are not required to be proven but defendant can seek to prove they did not know or were not aware as a defence or due diligence or other reason to be excused (but this evidential onus on defendant); (d) strict liability with no statutory defence provided – fault elements are not required to be proved and proof of physical elements is sufficient; (e) absolute liability – fault elements are not required to be proven, proof of physical elements is sufficient and liability still applies even if no intent, recklessness or negligence.

[70] This sub-section has been provided by Associate Professor Anil Hargovan.

[71] See, for example, editorial in the *Insolvency Law Bulletin*: (2021) 21(9&10) *Insolvency Law Bulletin* 102; Samantha Kinsey et al, King & Wood Mallesons, 'A spot-fire mentality to Australia's insolvency laws is still not the answer' (Web page, 29 September 2021).

[72] Law Reform Commission, *General Insolvency Inquiry* (Report 45, 1988).

[73] The submission builds on aspects of submissions made to this committee in 2014 by Professors Jason Harris, Christopher Symes and Colin Anderson of SCoLA (then CLTA). On that occasion, the authors recommended, inter alia, that the Committee review whether Australia needs a more nuanced set of insolvency procedures to deal with the different needs of large and small businesses in financial distress and insolvency.

55. Following the release of the *Review of the Safe Harbour Insolvent Trading Report* (**Panel Report**), it is a clear understatement to say that the time is ripe for a root and branch review of our insolvency laws which currently resemble a legislative maze.[74]

56. The Panel's Report offered compelling reasons to update Australia's insolvency laws for the 2020s and beyond. The Panel observed:

> one of the drivers of the Harmer Report was the acknowledgment that economic and social change are factors that indicate a need for review of insolvency law and procedure. There has been significant economic and social change in Australia since the publication of the Harmer Report in 1988. The way in which capital (both public and private) is sourced, and the globalisation of debt and equity capital markets, are just some illustrations of the ways in which Australia in 2021 is a very different place to Australia in the early 1990s.[75]

57. Moreover, it is also hard to quibble with the Panel's observation that any review should consider the different challenges faced by companies in the SME and mid markets compared to larger companies.[76] Once again, this echoes the criticism often made that a 'one size model' does not fit all.[77] Observations in the Panel's Report are also apposite to the former government's call for law reform options for schemes of arrangements.[78] It is difficult to disagree with the following submission made by the Law Council of Australia:

> There is much to be said for a broader review in relation to what reforms could be introduced to further support the restructuring of financially distressed businesses in the Australian context, particularly businesses other than large scale enterprises. Such a review could consider not only schemes of arrangement, but also whether further improvements could be made to the voluntary administration process in Part 5.3A of the Act, the restructuring process in Part 5.3B of the Act, as well as whether other processes could be adapted in this jurisdiction …[79]

58. Similarly, the reasons underpinning the call for a wholesale review of Australia's insolvency and restructuring procedures are captured in the following observations:

> The years since the Harmer Report have seen many 'ad hoc' changes to the law, most recently in response to COVID-19 … Along with the economic distortions caused by COVID-19, the overall result is a business/insolvency landscape in Australia - and the rest of the world - that is unprecedented in the 21st Century. After more than 30 years since the Harmer Report, it is submitted that the same reasons for the Harmer Report mean that the time has come for another comprehensive review rather than continued piecemeal reforms targeted at perceived shortcomings with unintended consequences.[80]

59. This submission echoes the calls above for a broader review, despite recent law reform with the introduction of Part 5.3B in the *Corporations Act* which provides for a new formal debt

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[74] The Treasury (Cth), *Review of the Insolvent Trading Safe Harbour* (Final Report, November 2021, tabled 24 March 2022). Consider the example given in the Panel Report at 85: 'To illustrate how layered and complex the provisions have become, … the new safe harbour carve-out for the SBR reforms is located in a part of the Act labelled section "588***GAAB***".

[75] Ibid 85 (citation omitted).

[76] Ibid.

[77] See, eg, (2021) 21(1&2) *Insolvency Law Bulletin* 2.

[78] The Treasury (Cth), *Helping Companies Restructure by Improving Schemes of Arrangement* (Consultation Paper, August 2021). See also Murrays Legal, 'Government's law reform of schemes of arrangement a "complete waste of resources when the core problem brewing is in the SME market"' (Web page, 14 March 2022).

[79] Law Council of Australia (Business Law Section), Submission to The Treasury (Cth), *Improving Schemes of Arrangement to Better Support Businesses* (17 September 2021).

[80] Samantha Kinsey et al, King & Wood Mallesons, 'A spot-fire mentality to Australia's insolvency laws is still not the answer' (Web page, 29 September 2021).

restructuring process for eligible companies.[81] An assessment of this recent law reform, below, demonstrates the issues arising from an ad hoc law approach to law reform.[82]

Background

60. Ad hoc changes to the law, particularly over long periods, have real consequences. In this context, unsurprisingly, Australia's insolvency framework has rightly been characterised in a recent report as 'an impenetrable quagmire that is scary, complex and unknown'.[83]

61. The recent approach to small business restructuring law reforms in Part 5.B of the *Corporations Act* serves to illustrate the point.[84]

62. The insolvency law reforms for small business were announced in late September 2020, introduced into Parliament in November, passed in December and came into effect on 1 January 2021 via the *Corporations Amendment* (*Corporate Insolvency Reforms) Act 2020* (Cth). It was introduced as a response to the impact of the COVID-19 pandemic on the national economy and provides for a new debt restructuring process for eligible incorporated small business, a simplified liquidation process for such businesses in a creditors' voluntary liquidation and a new 'class' of registered liquidator under the Insolvency Practice Rules.

63. Notwithstanding this significant development, there are serious concerns about the process used to introduce a complex piece of legislation with serious implications for stakeholders. The break-neck speed in which these significant reforms were rushed through parliament is regrettable. The haste in which the reforms were pushed through are captured in the following observation made by a Member of Parliament:

> Prior to the announcement, no small business group was consulted, and no insolvency experts or accounting bodies were consulted or engaged with by this government. And when the legislation regulations were released for consultation … stakeholders were given just four working days and a weekend to absorb and critique the complex reforms in this intricate area of law.[85]

64. An allied concern is the growth of regulations in support of the Act. This trend, of 'a thin stream of legislation meandering its way through lush fields of delegated legislation'[86] has, regrettably, become commonplace and does little for transparency, comprehensibility and certainty.[87]

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[81] As described in the Explanatory Memorandum, Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (Cth), the restructuring process is intended to provide a simpler, less expensive restructuring option for eligible small businesses. The Explanatory Memorandum states that 'the ultimate aim of restructuring is to have a plan in place which sets out an approach to repayment of the company's existing debts, thereby enable the company to stay in business and avoid being wound up': at 13 [1.4].

[82] For a wide-angle lens on insolvency law reform discussion, see Michael Murray and Jason Harris, 'Rebuilding the Structure of the Australian Insolvency System' (2022) 22 (1&2) *Insolvency Law Bulletin* 14.

[83] The Treasury (Cth), *Review of the Insolvent Trading Safe Harbour* (Final Report, November 2021). The Panel made 14 recommendations for reform to the safe harbour provisions in the *Corporations Act*.

[84] The following content draws upon Anil Hargovan 'Australian Insolvency Law Reform for Small Business — Janus-Faced?' (2020) 21 *Insolvency Law Bulletin* 5.

[85] Commonwealth, *Hansard*, House of Representatives, 8 December 2020 (Brendan O'Connor, Second Reading of Corporations Amendment (Corporate Insolvency Reforms) Bill 2020).

[86] Commonwealth, *Hansard*, House of Representatives, 7 December 2020 (Stephen Jones, Second Reading of Corporations Amendment (Corporate Insolvency Reforms) Bill 2020).

[87] See Commonwealth, *Hansard*, House of Representatives, 7 December 2020 (Daniel Mulino, Second Reading of Corporations Amendment (Corporate Insolvency Reforms) Bill 2020), where Dr Mulino remarked:

> It has been a rushed consultation process. Stakeholders had only five days to make submissions on the exposure draft of the bill. Five days for something this complex, this momentous, is not enough … so

Assessment

65. The discussion below offers critical comment on some aspects of the design principles underpinning the new Part 5.3B of the *Corporations Act* – namely, the potentially restrictive liability cap for small business, the unusual features of the proposed debtor in possession model and the questionable claim of achieving the policy objective of an overall reduction in complexity and costs.

66. **Eligibility of a small business**. As part of the eligibility criteria for a small business to rely upon the new debt restructuring procedure, the liabilities of the company will be a critical factor. The maximum amount of liabilities, and the manner in which it is to be calculated, is yet to be announced in the regulations. The Treasurer, however, has publicly announced a liability cap of $1 million.[88]

67. If implemented, it raises a concern that this cap is likely to be small and may not sufficiently accommodate any future changes in the economy. Economies are never static and, as noted by the Productivity Commission, 'macroeconomic conditions and population changes, along with broader government policy settings that influence the business cycle, can have an overarching influence on business set-ups, transfers and closures.'[89] This is reason enough to have a higher figure.

68. Furthermore, the proposed liability cap bears little or no relationship to the manner in which the government has defined small business in other relevant contexts, for example for purposes of tax concessions and for financial reporting.

69. In the context of accessing small business entity concessions, the ATO defines a small business as a sole trader, partnership, company or trust that has an annual turnover (excluding GST) of less than $10 million.[90] Previously, prior to 1 July 2016, the turnover threshold was $2 million. In the context of exemptions from the need to prepare financial statements, section 45A of the *Corporations Act* defines 'small proprietary companies' (as amended in 2019) as companies with at least two out of the following three characteristics:

    69.1. an annual revenue of less than $50 million (previously $25 million);

    69.2. fewer than 100 employees at the end of the financial year (previously 50);

    69.3. consolidated gross assets of less than $25 at the end of the financial year (previously 12.5 million)

70. Viewed in this context, the proposed liability cap appears to be low and should be reconsidered.

71. Against the ATO definition of a small business, small businesses account for 98.45% of all Australian businesses.[91] In 2013, 36% of small businesses had a turnover of $200,000 to less than

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much of the detail of what we're going to see is going to be in the regs. This is something we see as a somewhat concerning trend in a number of areas of regulation. Given the complexity of this reform and how serious it is, if there is a lot of detail in the regs it only reinforces the appropriateness of a statutory review and a sunset clause. The fact that so much of the detail is not going to be seen by this parliament when we vote on this bill reinforces the need for this parliament to insist upon additional protection.

For the importance of the key touchstones (transparency, comprehensibility and certainty) for legislative drafting and statutory interpretation, and the perils of ignoring them, see Stephen Mullette, 'Don't Go Chasing Waterfalls – Unfortunately s 588GAAA was Just Not Safe' (2021) 21(1&2) *Insolvency Law Bulletin* 27.

[88] Josh Frydenberg with Michael Sukkar, 'Insolvency reforms to support small business recovery' (Media Release, 24 September 2020).

[89] Productivity Commission, *Business Set-up, Transfer and Closure* (Inquiry Report 75, September 2015) 58.

[90] Australian Taxation Office, 'Small business entity concessions' (Web Page, 7 June 2021).

[91] Australian Small Business and Family Enterprise Ombudsman, *Small Business Counts – Small Business in the Australian Economy* (July 2019) 8.

$2 million with a slight decrease in 2016 to 34%, based on a 10,000 dataset of small businesses.[92] Notwithstanding that more than half of Australian businesses have a turnover of less than $200,000,[93] the figures suggest there may be a prima facie case to re-examine the current amount set for the total liabilities of a company seeking to enter the debt restructuring process.[94]

72. The proposed liability cap appears to be incongruous with the legal treatment of a small business for other purposes of commercial law.[95] Increasing the liabilities threshold to a higher amount, not necessarily to the same high thresholds under tax law and the *Corporations Act* discussed above, is likely to broaden the reach of the new law. It will significantly increase the chances of achieving the goals in section 452A which underpins the new Part 5.3B of the *Corporations Act* and the aspirational aim of achieving 'greater economic dynamism' in helping more small businesses to survive. Concerns about illegal phoenixing are legitimate, and are addressed under the draft legislation. It will also be incumbent upon the Small Business Restructuring Process (the **SBRP**) to act as gatekeeper against such abuse.

73. Finally, international comparisons show the proposed figure of $1 million will be significantly out of step with international practices, such as in the US and in Singapore. Access to the equivalent laws in the US (Chapter 11) requires an incorporated small business to have debts of less than US $2,725,625 after end of 27 March 2021 (currently temporarily raised to US $7.5 million)[96] and, for companies in Singapore, less than SG $2 million to enable access to the new streamlined process for insolvency.[97] Our laws, in this respect, should be competitive with the restructuring laws in other key foreign jurisdictions.

74. **Debtor in Possession Model**. The proposed debtor in possession model is akin to the Chapter 11 bankruptcy model used in the US, but with at least two key differences. Unlike the Australian proposal, access to Chapter 11 is not limited to companies with debts less than $1 million, evidenced above. Unlike the position in the US, the court is not given a central role, nor oversight function, in the new debt restructuring process in Australia.

75. The Janus-faced features of the proposed new law are most apparent when the role and functions conferred on the SBRP are considered. The new section 453E(1) confers an advisory role on the SBRP where they are expected to provide advice to the company to ensure that it meets the requirements of the debt restructuring process. This includes assisting the company in the preparation of the restructuring plan and making a declaration to creditors in relation to the proposed plan.

76. But the law reform goes well beyond conferring an advisory role on the SBRP. It also expects the SBRP to have a deliberative role where a variety of consents is required from them – such as consenting to the company entering into a transaction outside the ordinary course of business and consenting to the enforcement of ipso facto rights (new sections 453L(2) and 454P(7)). Furthermore, the SBRP is taken to be a company's agent (new section 453H).

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[92] Ibid 22.

[93] Ibid 8.

[94] Schedule 1, item 1, section 453C of the *Corporations Act* recognises that the threshold amount prescribed in regulations is amenable to change.

[95] Compare the Australian Restructuring Insolvency & Turnaround Association's submission which takes the opposite view and has called for a lower cap of $250,000: Submission to The Treasury (Cth), Insolvency Reforms to Support Small Business (12 October 2020).

[96] Nelson Mullins Riley and Scarborough LLP, 'The Small Business Reorganization Act: An Unintended Lifeline For Small Businesses Considering Restructuring Due to COVID-19', *Lexology* (Web Page, 24 August 2020).

[97] Insolvency, Restructuring and Dissolution (Amendment) Bill 2020 (Singapore); Ministry of Law (Singapore), 'Simplified Insolvency Programme' (Press Release, 5 October 2020).

77. It is difficult to reconcile the deliberative role expected of the SBRP when it is claimed by the government that a debtor in possession model will operate. If the latter prevails, query the need for the SBRP to be acting as the company's agent.

78. The Draft Bill indicates that section 9 of the *Corporations Act* will be amended to include the SBRP as an officer of the company. Consequently, all of the directors' and officers' duties under sections 180–183 (duty of care and diligence; to act with honesty and proper purpose and to avoid conflicts of interest), together with the accompanying civil and criminal liabilities for breach will apply. It is therefore important for the new law to clearly spell out the duties expected of the SBRP. Section 453E lists basic duties to advise the company and assist in preparing a restructuring plan to be put to the creditors but the further detail is left to the regulations, including their powers and their rights and liabilities. Only some sections expressly direct the SBRP to consider creditor interests when making particular decisions (new sections 453J(1) and 453L(5)). This regulatory gap leaves the SBRP vulnerable to potential civil and criminal liability for breach of officers' duties.

79. **Legislative Maze**. The government's penchant for 'clutter and complexity'[98] and law making through regulations continues unabated. Failure to fully address key substantive points, such as the eligibility criteria to use the restructuring process, together with the qualifications and duties of the SBRP, means that the regulations are expected to do the heavy lifting to make fuller sense of the new insolvency regime.[99] Consistent with recent practices, a regulatory morass can be anticipated which has potential to undermine the policy goals of the new law.

80. Instead of starting afresh, with a root and branch review of the operation of voluntary administration upon which large parts of the new Part 5.3B is modelled, the government has fallen into the trap of path dependency.[100] By its own admission, the Government noted in the explanatory materials to the Draft Bill:

> The new debt restructuring process draws heavily on the established voluntary administration framework in Part 5.3A of the Corporations Act and shares many of its features …[101]

81. It begs the question as to why the new Part 5.3B is modelled on a law that admittedly suffers from the following defects candidly acknowledged by the former government?

> The current insolvency system is a one-size-fits-all system that imposes the same duties and obligations … the current system lacks the flexibility to provide for small businesses for which complex, lengthy and rigid procedures can be unsuitable. The barriers of high cost and lengthy processes can prevent distressed small businesses from engaging with the insolvency system early …[102]

82. For sure, the government has introduced modifications to try and accommodate the specific needs of small businesses, but it cannot be said to have done so in a consistent and coherent manner. For example, as noted in many public submissions,[103] the government's failure to address the widespread use of trading trusts has potential to undermine the effectiveness of both the proposed

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[98] Cally Jordan, 'Unlovely and Unloved: Corporate Law Reform's Progeny' (2009) 33(2) *Melbourne University Law Review* 626, 635.

[99] Exposure Draft Explanatory Materials, Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (Cth) [1.134]–[1.136].

[100] See further Lucian Arye Bebchuk and Mark J Roe, 'A Theory of Path Dependence in Corporate Ownership and Governance' (1999) 52 *Stanford Law Review* 127.

[101] Exposure Draft Explanatory Materials, Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (Cth) [1.7], [1.12].

[102] Ibid.

[103] See, eg, Australian Restructuring Insolvency & Turnaround Association, Submission to The Treasury (Cth), Insolvency Reforms to Support Small Business (12 October 2020).

debt structuring and the streamlined liquidation process. It is anticipated that many small insolvencies will continue to require expensive court intervention.

83. It is regrettable that the government did not adequately seize a unique opportunity to fashion a new insolvency regime, sui generis, to fully accommodate the specific needs of small businesses. Instead, the end-user (small business community) is likely to be required to navigate a complex and opaque law that is currently drafted in a way that is not easily accessible nor easily digestible. Some core provisions, such as the eligibility criteria for use of the new restructuring law or the qualifications of the SBRP, will not be found in the primary legislation.

Neither Fish nor Fowl

84. It is regrettable that the fast-tracked reform process of such magnitude has not allowed proper opportunities for deep consultation. Nor was there any attempt by the government to consider the flow on effects of the Draft Bill and its potential impact on bankruptcy law, given that many small businesses have their debts secured by directors' personal guarantees. The rushed process carries a heavier risk of sub-optimal law reform.

85. It is hoped that Australia does not end up with a new insolvency legal framework that reflects the current proposals which, in essence, are neither fish nor fowl. They are largely modelled on the complex provisions of voluntary administration, with a trim here and there, and re-engineered as a saviour for small business.

86. The proposals could do with further trimming to reflect the more common scenarios that can be easily anticipated when dealing with small business. To illustrate, related party creditor transactions can generally be expected to be more prevalent in a small business setting. If so, query the utility of the current provisions which expect court action to be made to challenge voting by related party creditors. This often entails delays and added costs. An expedient solution, consistent with the underlying policy objectives of the reform proposals, would be simply to exclude any related party creditor votes.

87. The risks to insolvency law reform without paying sufficient attention to adopting a holistic approach are well documented. The warning sounded by Professor Fletcher to the approach adopted to UK insolvency law reform a few decades earlier (1986–2003) are apposite:[104]

> Piecemeal tinkering with the machinery of insolvency law may perhaps fall short of altering the core values on which the entire system is built, but may nevertheless give rise to unintentional, unwelcome consequences.

88. Similarly, turning to the piecemeal approach favoured by the government to insolvency law reform in Australia, Professor Harris made the following critical remarks which bears repeating:[105]

> I can't help bemoan the lack of big picture reform. Other jurisdictions are introducing new regimes, considering debtor in possession procedures … We should be asking the fundamental question of what we want out of a 21st century insolvency and restructuring legal framework?

89. It is questionable whether the current reform will simplify the law and reduce costs to the extent claimed. On current evidence, such claims made in the explanatory materials appear to be cosmetic and overstated. The ultimate proof, however, is likely to be found in the complex regulations accompanying the new Part 5.3B of the *Corporations Act*.

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[104] Ian F Fletcher, *The Law of Insolvency* (Sweet and Maxwell, 4th ed, 2009) 1-045.

[105] Jason Harris (editorial) (2016) 17(9–10) *Insolvency Law Bulletin* 166.

90. We await the next instalment to the package of reforms to the Australian insolvency framework. To guard against the prospect of the government letting a good crisis go to waste, it will be desirable for the government to commit to a root and branch review[106] of the operation of the new Part 5.3B after its implementation.

91. Should the evidence call for fundamental reform, it is hoped that the government will commit to a sui generis legislative effort, fit for purpose, rather than rely on tinkering with Part 5.B – which is modelled heavily on rebadged parts of Part 5.3A of the *Corporations Act*.

Selected issues for reform that are the subject of existing activity/impetus

92. **Review of the legislative framework for corporations and financial services regulation**. On 11 September 2020, the former Attorney-General referred to the Australian Law Reform Commission 'for inquiry and report … a consideration of whether, and if so what, changes to the *Corporations Act 2001* (Cth) and the *Corporations Regulations 2001* (Cth) could be made to simplify and rationalise the law'.[107] The Commission has produced one interim report, with a further interim reports due in September 2022 and August 2023. The final report is due by 30 November 2023.

93. **Review of the *Modern Slavery Act 2018* (Cth)**. On 31 March 2022, the Assistant Minister for Customs, Community Safety and Multicultural Affairs announced a statutory review of that Act.[108] The review should be completed by April 2023.

94. **Whistleblower provisions in the *Corporations Act***. The *Treasury Laws Amendment (Enhancing Whistleblower Protections) Act 2019* (Cth) made substantial reforms to the whistleblower protection regime under the *Corporations Act*. A review of the operation of that regime will be required in 2024,[109] and in the interim ASIC has conducted its own review of public and large proprietary company compliance.[110]

Further issues for reform

95. Members of the Society expressed views as to further issues for reform, which have not been addressed above. These include:

    95.1. mandatory training for first-time directors, provided by ASIC and/or accredited providers;

    95.2. financial services and whether the regulation of financial services should remain as Chapter 7 of the *Corporations Act* (the Australian Law Reform Commission's review of the legislative framework for corporations and financial services regulation, noted above, is focused on Chapter 7 and its consolidated final report will be available in November 2023);

    95.3. phoenixing;

    95.4. fintech regulation: blockchain and digital currency; and

    95.5. the BEAR regime, in particular whether it requires strengthening.

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[106] For a similar call, see Australian Restructuring Insolvency & Turnaround Association, Submission to The Treasury (Cth), Insolvency Reforms to Support Small Business (12 October 2020).

[107] Australian Law Reform Commission, 'Terms of Reference', *Review of the Legislative Framework for Corporations and Financial Services Regulation* (Web site).

[108] Australian Border Force, 'Review of the *Modern Slavery Act 2018* (Cth)' (Terms of Reference, March 2022).

[109] *Corporations Act 2001* (Cth) s 1317AK.

[110] Sean Hughes, 'Whistleblower Policies and the Compliance Gap' (Speech, 3rd Australian National Whistleblowing Symposium, 11 November 2021).

96. Should any of these matters be of interest to the Committee, further information can be provided.

Views on the Committee's work

97. As part of its preparation for this submission the Executive of the Society surveyed its membership on its views on the work of the Committee.

98. This question was met with a variety of responses. These spanned the spectrum from 'I read their reports with great interest' to comments indicating a lesser degree of engagement. Interestingly feedback was also received encouraging the Committee to 'be less cautious'.

99. Overall the Society strongly supports the work of the Committee and its efforts to consistently engage with industry, academia and a range of stakeholders in the interests of improved Australian corporations and financial services regulation.