

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Inquiry into Corporate Insolvency in Australia

Division: The Australian Small Business and Family Enterprise Ombudsman
Topic: Small Business Insolvency
Reference: Spoken
Senator: **Questions Submitted By**
1. Senator O'Neill
2. Senator Pratt

Question:

1. I ask you to take on notice the triggering of an action by banking or financial institutions or any other lenders, including equipment providers through financing? (p. 35, Hansard. Further clarification: what will trigger a lender to take action such as selling assets?)
2. How should regulators respond to that changing set of trends? (in relation to peak insolvency numbers following COVID) (p, 37, Hansard)

Answer:

1. A lender may take action when a consumer (an individual or small business owner) defaults on their loan obligations. The Australian Banking Association defines 'default' as failure to meet any of the terms and conditions of the contract.¹ Recovery action can include engaging a debt collection service or appointing a receiver to the company, which may result in a default judgment against the consumer for possession of a security property and/or repayment of the debt.

Loan agreements often provide a 30-day grace period to allow the consumer to correct their action before it becomes an event of default. This may include seeking to enter into a repayment arrangement with the financial firm. According to the Australian Financial Complaints Authority (AFCA), bankruptcy alone is not a sufficient reason for a financial firm to decline hardship assistance for a secured debt, provided the consumer can show that they would be able to repay the debt under a contract variation.² If the consumer is unable to fix the issue within the grace period, they will have defaulted on their loan obligations and the financial firm will generally be entitled to take action to recover the debt.

2. We recommend ensuring that regulators have adequate legislative flexibility to adopt a tailored approach in responding to changing trends in insolvencies, such as those observed during the COVID-19 pandemic. We understand that the existing lack of

¹ Australian Banking Association, *Banking Code of Practice: Setting the standards of practice for banks, their staff and their representatives*, 1 March 2020 (revised 5 October 2021), p. 58

² AFCA, *The AFCA Approach to financial difficulty: dealing with common issues*, p. 4.

flexibility in legislation is a barrier to providing customised responses. Small businesses will be better supported if relevant legislation allowed regulators to consider the unique circumstances and region-specific challenges on a case-by-case basis. This may result in better advice to the small business, allowing them to consider alternatives to liquidation, such as restructuring. Legislation could also consider greater flexibility to waive fees, such as the Australian Securities and Investment Commission's company registration and annual review fees, and freezing penalties in times of emergencies. This improved legislative flexibility will allow regulators to respond more swiftly to a changing set of trends in future emergencies.

Any reforms should also consider improving small and family businesses' direct access to regulators with operator support, at times when automated support is not appropriate or helpful.