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SENATE STANDING COMMITTEE ON

LEGAL AND CONSTITUTIONAL AFFAIRS

Tuesday, 23 January 2007

Members: Senator Payne *(Chair)*, Senator Crossin *(Deputy Chair)*, Senators Bartlett, Brandis, Kirk, Ludwig, Scullion and Trood

Participating members: Senators Allison, Barnett, Bernardi, Bob Brown, George Campbell, Carr, Chapman, Conroy, Eggleston, Chris Evans, Faulkner, Ferguson, Ferris, Fielding, Fierravanti-Wells, Fifield, Heffernan, Hogg, Humphries, Hurley, Johnston, Joyce, Lightfoot, Lundy, Ian Macdonald, Mason, McGauran, McLucas, Milne, Murray, Nettle, Parry, Patterson, Robert Ray, Scullion, Sherry, Siewert, Stephens, Stott Despoja, Watson and Webber

Senators in attendance: Senators Kirk, Ludwig, Mason, Payne and Trood

Terms of reference for the inquiry:

Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006

WITNESSES

Committee met at 9.16 am

CHAIR (Senator Payne)—Good morning, ladies and gentlemen. This is the hearing for the Senate Standing Committee on Legal and Constitutional Affairs inquiry into the Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006. The inquiry was referred to the committee by the Senate on 7 December 2006 for report by 8 February 2007. The bill proposes: to allow bankruptcy trustees to recover superannuation contributions made prior to bankruptcy with the intention of defeating the claims of creditors; to provide for certain rural support grants to be exempt from the property available to pay creditors in cases of bankruptcy; and to make minor technical amendments to clarify or improve the operation of the Bankruptcy Act 1966. The committee has received 13 submissions for this inquiry. All submissions have been authorised for publication and will be available on the committee's website.

I remind all witnesses that in giving evidence to the committee they are protected by parliamentary privilege. It is unlawful for anyone to threaten or disadvantage a witness on account of evidence given to a committee, and such action may be treated by the Senate as a contempt. It is also a contempt to give false or misleading evidence to a committee. The committee prefers all evidence to be given in public, but under the Senate's resolutions witnesses have the right to request to be heard in private session. It is important that witnesses give the committee notice if they intend to ask to give evidence in camera. If a witness objects to answering a question, the witness should state the ground upon which the objection is taken, and the committee will determine whether it will insist on an answer, having regard to the ground which is claimed. If the committee determines to insist on an answer, a witness may request that the answer be given in camera. Such a request may of course also be made at any other time.

[9.18 am]

ANDERSON, Dr Michaela, Director, Policy and Research, Association of Superannuation Funds of Australia

PRAGNELL, Dr Brad, Director, Policy and Best Practice, Association of Superannuation Funds of Australia

CHAIR—Welcome. Do you have any comments to make on the capacity in which you appear?

Dr Anderson—I am deputy CEO of the Association of Superannuation Funds of Australia.

CHAIR—The Association of Superannuation Funds of Australia has lodged a submission with the committee, which we have numbered 6. Thank you very much for that. Do you need to make any amendments or alterations to that submission?

Dr Anderson—No.

CHAIR—I now invite you to make a brief opening statement. At the end of that statement, we will go to questions from members of the committee.

Dr Pragnell—The Association of Superannuation Funds of Australia, ASFA, is pleased to appear before this committee in its inquiry into the Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006. ASFA is a non-profit, non-political, national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. Our members, which include corporate, public sector, industry and retail superannuation funds, account for more than 5.7 million member accounts and over 80 per cent of superannuation savings.

ASFA welcomes this bill. It represents a significant advance over earlier attempts to introduce legislative change in this area. In particular, the September 2005 consultation paper on the effects of bankruptcy on superannuation contributions articulated a regime that would have imposed considerable cost and complexity on superannuation funds and, by extension, all fund members.

It needs to be remembered that superannuation fund trustees will ordinarily be a third party in a personal bankruptcy situation—the proverbial meat in the sandwich between the bankrupt and those acting on behalf of creditors. Unlike the over-engineered September 2005 proposal, the current bill seeks to minimise any active role for the superannuation fund trustee. Super funds will be required to respond to any payment and freezing notices issued to them after the courts have determined that the bankrupt superannuation contributions were made with the intent of defeating creditors. This approach means that superannuation funds trustees will not need to test the bona fides of particular contributions, undertake complex calculations or enter legal proceedings. However, superannuation fund trustees may take legal action to contest notices received.

The bill also contains a number of other positive features. It sets out clear time frames within which a superannuation fund trustee must take specific action. There is specific recognition that contribution amounts may have been reduced due to fees, charges, taxes or

negative investment earnings. The superannuation fund trustee is also protected from civil and criminal action and regulatory breaches where it acts in good faith and in accordance with notices and orders issued under the act.

Despite the overall soundness of the approach taken and the many positive features of this bill, there remain areas that ASFA believes do require attention. In particular, the bill rightly seeks to ensure that the trustee of the superannuation fund does not bear any loss resulting from fees, charges or taxes paid in respect of that contribution. If a superannuation contribution has been made and the notice seeks to recoup that contribution, the final amount received by creditors is to be adjusted to take into account that fees, taxes and so forth may have been paid on that contribution. Simply put, the bankrupt contributed $1,000 to defeat creditors and the notice has been written up to recoup the $1,000. The final amount received on behalf of creditors might be, say, $820—maybe a bit more or a bit less—to reflect the fees, taxes and so forth that may have been paid. We strongly support this policy objective. To do otherwise would adversely affect other members of the fund.

In the bill, this is done through a multi-step process. First, the official receiver provides a notice of payment to the superannuation fund. Second, the superannuation fund pays the total amount of the contribution as specified in the notice to the trustee in bankruptcy. Finally, the trustee in bankruptcy is then required to pay back to the superannuation fund an amount equal to the fees, taxes and charges debited in respect of the contribution. As it is only the superannuation fund trustee that is aware of the fees, taxes and charges debited in respect of those contributions, it would be far simpler if the law permitted the superannuation fund trustee to pay only the net amount and to advise the trustee in bankruptcy of the reason for the reduction in the payment.

Making amendments in this area could also overcome another technical problem outlined in our submission whereby the superannuation fund can inadvertently be paid twice. There are also some other minor concerns with account freezing notices that we have outlined in our submission. Despite these relatively minor issues, ASFA believe that the approach taken in the bill is a significant improvement over earlier proposals, and the government should be commended for taking a pragmatic and workable approach.

Lastly, ASFA does have concerns about the capacity of the industry to implement the necessary changes to administration systems, processes and procedures to deal with processing payments and freezing notices within a relatively short time frame. Superannuation funds have limited resources. Simplified superannuation proposals and the anti money laundering counterterrorism financing changes both come into force during 2007 and represent significant administrative challenges to be faced by funds and administrators. ASFA therefore requests, in consideration of these other changes, that the substantive proposals contained in this bill commence on 1 January 2008. We do recognise, however, that the regime must apply to contributions that were made on or after 28 July 2006. We appreciate this opportunity to appear before the committee and welcome any questions.

CHAIR—Thank you very much, Dr Pragnell. Dr Anderson, did you wish to add anything?

Dr Anderson—No.

CHAIR—Just an initial question, then. You said in your remarks, Dr Pragnell, that ASFA welcomes the legislation and so on.

Dr Pragnell—Yes.

CHAIR—Can you tell us what involvement you had in the consultative processes?

Dr Pragnell—We were quite involved in discussions with Treasury and ITSA in earlier consultations back in 2003, 2005 and more recently around this bill. I think generally we have found the process has been quite good. Those agencies have been very open to listening to industry concerns. In respect of cost and complexity we were quite pleased, as I mentioned in our opening remarks, to see that there was a rethink around the 2005 proposals, which would have imposed considerable cost and complexity. Other than maybe finessing certain aspects of this bill, we think that the regime is definitely a significant improvement and definitely achieves the policy objectives that were set out back in 2003.

CHAIR—The two broad aspects of your propositions to the committee, that small number of technical changes or issues, and then your observations in relation to a commencement date—have you engaged on those issues with the relevant government departments? What has been the response?

Dr Anderson—I think we have raised those issues but only fairly recently.

CHAIR—Do we have any feedback?

Dr Anderson—To our knowledge, I do not think we have feedback on those—

Dr Pragnell—Not on those specific issues.

Dr Anderson—specific issues, no.

Dr Pragnell—We were consulting primarily on the broad structure of the legislation, and I think that is what our primary concern is about. It really was not until the bill came out and we actually did some analysis and consulted with our members on some of the technical issues that a lot of these matters came up. So I would say they are relatively minor and I think they are fixable.

Dr Anderson—The main issue for us has always been to remove the trustee from having to make the decisions, to be really involved in any dealings with the bankrupt person, and I think we have achieved that.

CHAIR—Thank you very much. We will go to questions from my colleagues. Senator Ludwig.

Senator LUDWIG—Thank you. Have you had an opportunity to look at how the bill will operate with the new superannuation rules that permit people to make significant contributions now? The bill may not have foreseen the superannuation changes that have recently been announced, because it talks about out-of-character payments. What we are going to find, I suspect—or, at least, what Treasury is hoping for—is that there will be significant out-of-character payments and expenses put into superannuation funds. Have you turned your mind to how you will operate with that? In this instance, you will be a passive bystander—the payments will be made and you will watch them come in and then it is a matter for others to determine how it will operate.

Dr Anderson—I think that goes to my earlier point that in fact we do see the trustee as removed from that—although, just as an observation, you would have to say that anything that appeared to be within the rules for the new amounts that can be contributed would have to be examined very carefully to see if it was out of character.

Senator LUDWIG—What role will you as an organisation play in that—consulting and advising your members?

Dr Anderson—Our members will not be making that decision.

Senator LUDWIG—No, I understand that. But will they be passive in that sense—passive bystanders? I do not think so. They will have some interest in what is happening to the superannuation.

Dr Anderson—I would imagine our advice would be that they remain passive. This has always been the thing that our members have raised with us—that they do not want to become involved in making these sorts of decisions. If we go back to our members and find that they now want to become involved, that would be quite an about-face.

Senator LUDWIG—What advice would you be providing to your members in terms of this bill?

Dr Pragnell—As Dr Anderson has tried to outline, the bill, the regime, effectively means that decisions in respect of intent are made elsewhere by the courts, and that superannuation funds will need to develop systems and procedures to respond to those notices. In the past we have assisted our members through best practice papers on legislative changes that are similar in areas such as family law, for instance. We may be able to provide some kind of assistance there.

The other issue for us is to indicate to our members that they have certain legal rights under this bill. They have the ability to go to the courts and, as we mentioned, they should have the ability to go to the official receiver as well. It is really about the trustee not wanting to get embroiled unnecessarily in what are effectively dealings between the bankrupt and persons acting on behalf of the creditor. As much as possible we want the trustee to be a third party that effectively does what it is told, as opposed to having to get involved in making difficult judgement calls or being caught between disputing parties.

Dr Anderson—I do not think the trustees would have any difficulty with providing information. We have always said that trustees will provide information but they will not make decisions. Part of that is that the trustees actually have very little knowledge other than knowledge about contributions made and the timing of those contributions. Beyond that, they do not know very much about the financial or other affairs of most of their members.

Senator LUDWIG—I suspect they might have to get on top of some of that with the new AML/CTF legislation coming in.

Dr Anderson—Yes. I would not—

Senator LUDWIG—I would be surprised if you were not going to advise your members about the AML/CTF legislation requirements to know your customer.

Dr Anderson—I would imagine that some of the things you would need to know about your customer would not always be relevant in this case.

Senator LUDWIG—I will not imagine what it is. There are specific requirements under the new legislation, and I am sure you will take the opportunity to advise your members accordingly in respect of that. The point I am also trying to draw from you is this: if you say you are passive in the sense that you will be advising your members to be passive and that you will be able to provide information as requested, what is the scale of that call? What has it been like in the past? Are you able to say how much that amounts to?

Dr Anderson—None at all.

Dr Pragnell—We could not provide you with figures on that.

Senator LUDWIG—Why should I then accept your submission that you require a deferred start-up date if you cannot tell me what impact it may have on your members and on the amount of work they might have to do, and that they are going to be passive in that sense?

Dr Anderson—No matter how many people would be involved in this, the trustees will have to set up systems as though everyone will need the system. It is the same with other issues as well: you may not know how many people will need the process or the system but you have to make it available.

Senator LUDWIG—I accept that you would have to set up systems. Similarly, you will have to set up systems for AML/CTF, but it will be the trustees. What I am trying to draw from you is what is already there. It may already be in train. They may already have systems in place, because obviously there has already been a call for this type of information to be brought forward. There have already been disputes about it in the past. I do not know—I am really in your hands in this instance. You have to be able to convince me and tell the committee that there is an impost—it is significant—and the scale of it and that it will require a delay. You have not been able to make that plain to me as yet.

Dr Pragnell—In terms of the significance, I think the main feedback that we have been getting from our members is that to implement simplified super is an all-hands-on-deck undertaking and, similarly with AML/CTF, that the industry's resources are stretched to a significant degree. We are also having to get online other initiatives that involve systems changes and to do it appropriately, to do it right, and not just to bolt something in which we are going to have to fix up six or 12 months later because we did not do it right the first time.

Our members really would appreciate some additional time from when this bill becomes an act to be able to work through what is required. Even at this point I think they are going to need to work through what these notices are going to look like, how they are going to receive the notices, how they are going to be dealt with, what processes they are going to put in place to deal with them, how the moneys are going to be paid out and how they are going to record that data. So coming out of this are a number of systems issues that will require some level of at least one-off activity from the trustees. I think that is what this kind of regime actually does. Once you set it up, it kind of rumbles along in the background, like everything else. But the start-up of it does require a reasonable burst of resources. I wish I could provide you with some more detailed costings or scale, but—

Senator LUDWIG—So do I.

Dr Pragnell—We would like to as well. But our members are heads down on simplified super and on AML/CTF at the moment; they are trying to get their heads around the demands of those very significant reforms and they have to do things reasonably quickly and be reasonably demanding to make sure that all works.

Senator LUDWIG—I accept that. What I am also concerned about is the delayed implementation date—you are aware that AML/CTF has a phased implementation—

Dr Pragnell—Yes, that is exactly right. I know. But they already have to do things.

Senator LUDWIG—What you might be doing is pushing it all down to one point into the future, where it still collides and requires a significant amount of interaction to get right.

Dr Pragnell—From where we are coming from as an association, we really do want to communicate to our members—and I know, Senator, you have been quite involved with this—about the enormity of AML/CTF, about the challenge that it represents to funds and about the fact that, yes, there is this 24-month phased implementation but that it is a serious and demanding undertaking that will require a lot of work and a lot of resources to be devoted to it to do properly. I think that is something that we want to communicate to members: it is not something you worry about in 2008; it is something you should be thinking about right now, and I think our members are. Our members are definitely thinking about it now, but it is definitely a message that we want to keep up with them.

Senator LUDWIG—Are you able to supply a rough guide of what call is being made by creditors or trustees on these superannuation funds at the moment—in other words, the scale of work that they are already involved in? Even if it is anecdotal, I imagine you would have some sort of understanding from your members. The committee has a short turnaround, as I understand it. You could have a look at your records and see what you have. If you cannot then I accept that as well.

Dr Anderson—We could try, but this is not an area, we have discovered, where anybody keeps records centrally. It is a thing that happens every now and again and in some very large funds it happens reasonably often, but as a percentage of a million members it is probably not a lot. But it is interesting that it is something we have not been able to get a lot of data on.

Senator LUDWIG—I will reverse it then: do you deal with complaints on behalf of your members?

Dr Anderson—No.

Senator LUDWIG—They go directly to ITSA or wherever else.

Dr Pragnell—No. Are you talking about—

Senator LUDWIG—If there is a problem. We will take this as an example. If there is a matter that looks like it is going to head down the Cook v Benson road—somebody might say that this is a creditor chasing money from a superannuation fund. The person puts their hand up and says: 'I don't think this is right. Can someone help?' or 'I want to complain about where this process is being taken.'

Dr Anderson—As a member of a fund they have a right to go to the super complaints tribunal about a decision of the trustee. I am not quite sure whether this would fit there. Looking at the data that comes out of the tribunal, I do not remember if this is a category. I presume where it could become an issue with the tribunal would be around administrative issues, if they were taking issue with the trustees' administration rather than the decision. It is a strange little bit of our business. Nobody documents it well. It is probably not particularly well understood on a systematic basis. This legislation will probably help considerably in dealing with it better.

Senator LUDWIG—Thank you.

Senator MASON—I have a legal question. You will have to help me here because my only joining with bankruptcy law was a long time ago at law school, and it was short and quite tragic. Are the words 'out of character' to determine whether contributions have been made by a bankrupt with the intention to defeat creditors words with a common legal parlance?

Dr Pragnell—They may be elsewhere but not in the superannuation context. They may be in bankruptcy law but, again, I do not claim to have knowledge of bankruptcy law. Some of the other witnesses might be able to illuminate on that.

Senator MASON—I just wanted to know whether there was a legal precedence for what that meant.

Dr Anderson—It is not a term that we are familiar with.

Dr Pragnell—It is not used in the superannuation context ordinarily.

Senator MASON—To your knowledge, have there been many instances where bankrupts have tried to avoid their creditors by placing money in superannuation? Is this a common problem?

Dr Anderson—Only on hearsay. I think it has been an issue but it is not something that has been massively talked about within the superannuation industry.

Senator MASON—It has not been spoken about in the superannuation industry?

Dr Anderson—It is not a major issue.

Dr Pragnell—From our perspective, the issue does come up, obviously, but it is not something that occupies an inordinate amount of funds' time and resources. I think that is what we are trying to say. It obviously happens but maybe like in some areas of the law, because there was not necessarily a clear legal framework, lots of things happened but they happened in a lot of different places.

Senator MASON—Yes.

Dr Pragnell—There would be direct approaches, things would go to the courts, things would happen here, things would happen there, so it is hard to get a feel for the depth and breadth of what actually is happening. It is a bit like family law in a sense. There were always family law disputes in the past where superannuation was involved but it popped up in different contexts. It might appear in the courts, it might appear here or it might appear there,

and it was always a bit all over the shop. Now we have a framework that actually deals with that. This is similar in that sense.

Senator MASON—It was not, as you referred to it, 'overengineered' was it? Or was that different?

Dr Pragnell—The 2005 proposal for bankruptcy was definitely overengineered.

Senator MASON—It is a lovely word. Thank you.

CHAIR—As there are no further questions, I thank the witnesses for appearing, and for their submission.

[9.46 am]

ARNOLD, Ms Kim, Technical Director, Insolvency Practitioners Association of Australia

COOK, Mr Paul, Deputy President, Insolvency Practitioners Association of Australia

LOTZOF, Mr Mike, Chief Executive Officer, Insolvency Practitioners Association of Australia

CHAIR—Welcome. Do you have anything to say regarding the capacity in which you appear?

Mr Cook—Yes. I am also the trustee in the case Cook v Benson.

CHAIR—Thank you. I understand that you have not lodged a submission with the committee. I ask you to make an opening statement and we will go to questions after that.

Mr Cook—The Insolvency Practitioners Association of Australia welcomes the opportunity to appear this morning to discuss the Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006. The IPAA is an independent self-governing organisation that represents professionals who specialise in the field of insolvency. We have over 1,200 full and associate members, including accountants, lawyers, bankers, credit managers, university professors and other professionals with an interest in insolvency. We provide continuing education forums for members by way of discussion groups and conferences. We have a quarterly magazine called the *Australian Insolvency Journal*. We also consult with regulatory bodies such as ASIC and ITSA in the development of standards which our members must follow. We liaise and work with government bodies, such as the ATO and the Department of Employment and Workplace Relations. We are also active contributors to discussions on reform of the Australian insolvency laws and other insolvency related issues.

We welcome any legislative amendments which provide trustees with practical, fair and enforceable powers to recover assets for the benefit of creditors. With any reform package, the IPAA's main concern is that the amendments be simple, cost effective to implement and clear cut in their interpretation. The IPAA is supportive of the amendments proposed by the bill in respect of the recovery of superannuation contributions made prior to the bankruptcy with the intention of defeating the claims of creditors. We do believe that there are benefits in how the bill has been drafted in that the methodology is similar to that used for existing recoverable property provisions. However, we do hold some concerns in respect of the pattern of what we describe as the 'pattern of making contributions', which was referred to by senators and previous witnesses—the principle when determining the transferer's main purpose.

This principle does not give the trustee the same level of certainty as to whether the payment is void or not as the previously proposed threshold method. We recognise that, with time, case law will develop guidelines around this principle which will allow trustees to identify with more certainty what the position may be in respect of a payment. At the hearing we are attempting to articulate the views of our members, who represent a wide cross-section of the professional insolvency community.

Following on from the previous speakers, we concur that the 2005 consultation paper was an overengineered process and we were aware that something like 28 pages of legislation would have been required for effectively one section. In our view, that is ridiculous and so we welcome the modified approach that has been put forward. We are very happy to answer any questions the committee has.

CHAIR—Thank you very much, Mr Cook. Mr Lotzof and Ms Arnold, did you wish to add anything?

Ms Arnold—No.

Mr Lotzof—No.

CHAIR—Perhaps to start with you could outline for the committee whether the IPAA was engaged in the consultation process that led to this bill.

Mr Cook—Yes. It is effectively the secretariat for the Bankruptcy Reform Consultative Forum and I have been on it for about six years. There has been a lot of consultation. The main consultation was really put together with the previous reform package dealing with the doctrine of 'relation back' and trust breaking provisions. These two were taken together and the superannuation dropped off a bit in the consultation process because there was complexity. The level of consultation with the superannuation industry has been very minimal. I am not saying that as a criticism; it is just that most of our work in the consultation process has been with the government, talking about tables on reform, but we have not tended to have one-on-one consultations with the superannuation industry.

CHAIR—Mr Cook, just to clarify, do you mean your organisation has not—

Mr Cook—Sorry—our organisation. I should correct that, yes.

CHAIR—You do not regard that as a problem though?

Mr Cook—I do not think so. I have heard the comments today and I can make some comments if people ask me some questions about that. I do not see it as a major problem. We became concerned about the level of complexity and to some extent retreated from part of that consultation process when it became so complex. We thought, 'The superannuation industry has to sort itself out and then we will make a comment when it is a little less complex.'

CHAIR—I see. I have two other questions. Going to the concerns that you raised around the point of the pattern of making contributions, have you raised those with the government agencies?

Mr Cook—Yes.

CHAIR—What response have you had?

Mr Cook—I understand the response. It is a balance between how you deal with the complexity and with something that is more pragmatic. As trustees administering estates, the more certainty, the less cost and the more we turn to creditors because we know that we do not have to then go and do research. This is a very subjective issue and all of the questions that were raised before are questions that trustees ask and will ask every day about what is out of character. Senator Ludwig asked a question about superannuation contributions in this window of opportunity, yet they will be issues.

CHAIR—Are you comfortable with the commencement date?

Mr Cook—Yes. We are happy to begin as soon as possible. Our view is that, since the Cook v Benson statement came down on 16 September 2003, it is fair to say that the industry has been on notice for quite some time that there are changes in this area. Trustees at the moment write to the superannuation funds about information because, if you do something to fool creditors, those funds are available. This change is about affecting something where an anomaly popped up. That is not to say that trustees do not already write to trustees who receive the funds at the moment.

Senator KIRK—Thank you very much for your comments here today. Seeing as you were the plaintiff in the matter of Cook v Benson, I was wondering whether or not you might be able to outline for the committee what the High Court decided, the problem that resulted and how this bill seeks to remedy that.

Mr Cook—In summary, Mr Benson went bankrupt in 1992. My view was that moneys were knowingly put aside to defeat creditors. My belief was that he was advised by his financial advisers to do it. I attempted to then overturn that transaction. We went to court, where I won in the first instance but then lost in the full Federal Court and also in the High Court. The basis for that was that it was accepted that it is valuable consideration if somebody takes your money and says to you, 'I will look after it and try to improve it.'

Senator KIRK—So in that case they were superannuation contributions, I assume.

Mr Cook—They were deemed to be superannuation contributions that met the criteria to exempt it from recovery. You can recover money that has been put aside to defeat creditors where there has not been valuable consideration—that is, I give you my house and you do not pay me anything for it or it is undervalued. This is a case where superannuation moneys, for all intents and purposes, are effectively owned by the individual, who puts them into a fund for tax and other reasons and that fund says, 'I'll look after them,' and charges a fee—and that is a valuable consideration. That is what the High Court held. Then the government said: 'It seems that is not appropriate. Let's go about how we fix it.' It was seen to be fixed amongst a number of other reform ideas—and here we are today.

Senator KIRK—Was it a common practice, or is it a common practice now?

Mr Cook—Let me put it this way: I believe every financial adviser would know of this case and in their checklist of discussion with their clients ought to have some regard for asset protection planning and, if you like, loopholes. Whilst we do not necessarily see significant prevalence of large amounts of money moving to super funds, it is foremost in everyone's mind that you can do this; this is a loophole.

Senator KIRK—If this bill is passed into law, how will it impact on industry generally—not so much your industry but the way that things are practised out there in the—

Mr Cook—I think it is deterrent legislation. I think that, together with the retroactive statement that this is going to start from 2003—or whatever the date is; I have forgotten it—it sends a clear message that this is not on. So it is a deterrent. The question was asked: is it prevalent; does a lot of it happen? Our experiences are that entrepreneurs by nature do not like to give up cash and they do not tend to put money into super because they can gear it and use

it for other purposes. But it is there. As Senator Ludwig says, you have the opportunity to put funds into a super fund at the moment. Is it out of character? I raise this question at seminars that we attend on a professional basis: if your financial adviser says to you, 'Now is a good time to put a lot into super for your benefit,' is that out of character? Is it reasonable to assume that is the reason why he has done it? What I have learnt in life is: do not go to court for justice. The words 'reasonableness' and 'pattern' are open for interpretation. Having said that, I say this is much better than 28 pages of legislation that are very complex. This is probably a fair balance.

Senator KIRK—Has that phrase 'out of character' been subject to judicial interpretation in any other context? Is there any other indication as to how that will be interpreted?

Mr Cook—I am not aware of any, but I do not know if Kim—

Ms Arnold—I could not tell you.

Mr Cook—It is one of those subjective things. It starts off by saying: is it reasonable to assume that the main purpose of it was to do this? And then there is a definition of 'reasonableness', and it is not 'beyond reasonable doubt'; it is what the common man or woman would think about why they did this.

Senator LUDWIG—Will it be effective? Will it work? Take a look at the simplified super rules and the advice by financial planners. It is a sensible thing to do to provide advice to people that they should have money in super. There is now no RBL, so if you are in middle age and are a successful businessman it is not an unsound practice to put a significant amount of money into super—at any point, whether it be now or in the next couple of years, given that at retirement at 60, if you draw out an accumulation fund, you get a favourable tax treatment. In your view, how will you be able to differentiate between the sound practice of putting money into super and cases where it might be done to avoid paying creditors?

Mr Cook—I think it will be pretty successful. I will give you a couple of analogies. If somebody puts $5,000 into a super fund before they go bankrupt and they have never done it before, it is unlikely that we will recover that, from a pragmatic point of view, because the costs associated with fighting the amount of $5,000 will probably exceed the benefit. If a lot of small bankrupts put $5,000 in, I do not think it will be effective. Does that undermine the integrity of the whole bankruptcy system? I do not think so. At the higher end there will always, in our view, be people that find loopholes. There are always people that are pushing the envelope at the top end. Do I think we will stop those? Not any more or any less frequently than we are at the moment. Do I think that it is generally going to be successful? Yes, I do, because generally most people do not like parting with cash, especially when they come into financial difficulty.

The reality is that bankrupts are generally nice people who get into unfortunate situations. They do not set out to defeat. There is a percentage, and it is low, of people that we would describe as crooks. They are there, and when you come across them it is not great. But those people that really do try and pay all their debts do not tend to whack lots of money into super just before, because they do not have it and they would rather spend it somewhere else because they think that they will pay all their creditors. When most people come in and see practitioners the first thing they say is: 'I'm in trouble. I want to pay all my creditors.'

Usually, in most cases, they cannot. But many of them start off with a genuine statement believing that. I do not know if that answers your question.

Senator LUDWIG—It will not necessarily trouble the crooks, then. What you have effectively outlined is that the innocent bystander, the person with $5,000, will not be troubled by the legislation, and I can see why you would not pursue it. It generally would not trouble those people who are bankrupt by circumstance either because they would not generally be doing this. So it leaves us with the crooks. You would think the legislation is designed to attack those people. You are suggesting, as I understand it—or you can help me overcome this—that those people are going to do it. So the loophole remains for those, by and large.

Mr Cook—I am sorry if I misunderstood. I think it will be effective in that because the legislation is there. We would have to go to case law to find out, though, because of the term 'pattern of behaviour out of character'. We need a case that says, 'This is out of character,' and is more definitive. We will have to run cases. Those cases may have to be funded by the Commonwealth, and they may be prepared to do that.

Senator LUDWIG—What if the courts take a case-by-case examination? That is what it seems to suggest to me—that this type of bill will require a case-by-case examination rather than a determination of those words in a legal sense. The High Court may come back and, if you get leave and the case goes through, determine it one way or the other. They might say it is a matter for the High Court. But they might not put down a principle that you can then use in other cases. It simply seems to me that the language could be used on a case-by-case example, in which case you will have more litigation. Do you think that is a likelihood?

Mr Cook—No. My view is that trustees will be keen to take these cases on. It is pretty obvious what is out of character in one respect—you can see the elephant in the room. Then you have to go through the process of recovering. If you have a litigious bankrupt on the other side, you will take advantage of all the processes along the way. But I do not think it is that hard to spot an inappropriate pattern, I have to say.

Senator LUDWIG—Not everybody likes to recognise the elephant in the room, though.

Senator TROOD—Is that the point, Mr Cook, that you were alluding to in your opening remarks when you talked about the need for the level of certainty in relation to trustees?

Mr Cook—Yes.

Senator TROOD—It raises the question of whether or not—rather than waiting for the case law to develop, which is obviously one way in which you can approach any degree of legislation—the legislation itself might go further in trying to define and narrow the areas in which there might be a measure of confusion or uncertainty. Do you have a view as to whether or not it might be preferable for the legislation to go somewhat further in narrowing the areas of ambiguity?

Senator MASON—To be more prescriptive. Is that right?

Mr Cook—It would be great. It is a trade-off. There has been consultation on this. There has been discussion about how much further you go. It is one of those difficult balancing things. We would love it to be more so. We would like to avoid those other issues of having (a), (b) and (c) by saying: 'Here is an example in the legislation. If it fits this pattern, it is

that.' Generally, people will say, 'This is not out of character.' For example, with the latest, where you can put up to a million dollars in, they will say: 'It is not out of character. I put a million dollars in. The opportunity was there. I did it for my retirement. It just coincided with a time when I was in financial trouble. That wasn't the reason.' We will say, as trustees, 'That is a load of rubbish,' but we will need to gather the evidence and take it through to case law because they will say, 'It is not out of character.'

Senator TROOD—Have you had discussions on that point about perhaps extending the legislation to try and avoid some of these ambiguities?

Mr Cook—To put it into context, we have not had significant discussions because the changes to super came out at budget time. But, from consultation in consultative forums, the relevant stakeholders are aware of our views on that.

Senator TROOD—Do you have any particular views that you want to express to the committee on that point regarding some perhaps very specific ideas?

Mr Cook—To define them?

Senator TROOD—Yes.

Mr Cook—No, it is too hard! We are happy to go away and think about that and give a further submission on it. There are lots of other things on our agenda; the corporate law reform is taking precedence. Generally, in the whole superannuation area, it is very complex. We have not tended to get right into it. There were previous models put up. We examined those. All we are saying is that for the person who has to actually collect the money there is that uncertainty. You are asking me: 'Can I can fix that?' I cannot say off the top of my head.

Senator TROOD—I will leave it with you. I appreciate that it is complex. We do not have a lot of time to deal with the bill, so if it is beyond your ken and ours to deal with it in the time that is available then I understand. But if you have some thoughts on the matter which might be helpful to the committee then I would appreciate you sending them along.

CHAIR—Mr Lotzof, Mr Cook and Ms Arnold, thank you very much for attending today and for your assistance to the committee. We look forward to seeing what you come up with, Mr Cook.

Proceedings suspended from 10.08 am to 10.21 am

LHUEDE, Mr Michael, Chair, Bankruptcy Subcommittee, Law Council of Australia

CHAIR—Welcome. For the *Hansard* record, would you please state the capacity in which you appear before the committee today.

Mr Lhuede—I am a partner of Piper Alderman. I am appearing on behalf of the Law Council of Australia and also on my own behalf. I think my personal submission, by way of background, was received yesterday.

CHAIR—It was. The Law Council has lodged a submission which the committee has numbered 7. Do you wish to make any amendments or alterations to that submission?

Mr Lhuede—No.

CHAIR—I note that the number of your other submission is No. 11. I invite you to make an opening statement in relation to the legislation and then we will go to questions.

Mr Lhuede—On behalf of the Law Council of Australia and in my own regard, I thank the committee for the opportunity to attend today and to provide some feedback in relation to the Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006. The reason for the bill arose from the case of Cook and Benson and the implications that arose from that case. The Law Council and I formed the view very quickly that it left it open for probably the single biggest loophole in bankruptcy legislation, which would facilitate people wishing to defraud their creditors to do so quite simply and efficiently without any recourse against them. While we have not seen any cases since the Cook and Benson matter, it has certainly been a matter of public notoriety that this loophole exists. We have advocated since the findings in that case that something be done to close that loophole.

There were extensive consultations undertaken by the office of the inspector-general. Out of those consultations came an initial proposal which, from the Law Council's perspective, was thought to be quite cumbersome. The current proposal derives from submissions we had made earlier on in the piece; that is, that the means by which you could fix the problem are relatively simple, which is essentially what the legislature is now adopting. In that regard, we think that the changes are good and are needed. We think that the provisions are consistent with the model of the act and, in that regard, we support them. There are a couple of minor technical issues that the Law Council noted in its submission. They are minor and technical, but I do think that they should be addressed now.

I would submit that there is still one inconsistency in the act. This inconsistency was alluded to in the Law Council's submission at page 3, point 2. It relates to the level of protection afforded superannuation upon the bankruptcy of a member of a fund. It is that, if the moneys accrue to the member and the member immediately thereafter goes bankrupt, those funds would be available to creditors. For the life of me, I cannot see any rationale for that, and it does appear to be inconsistent with the general public policy of extending protection to superannuation payments upon bankruptcy.

CHAIR—We can pursue that latter issue with the relevant government departments. You have raised some particular issues about the use of the word 'compliance' and other technical

matters. Have you raised those matters with the Bankruptcy Reform Consultative Forum, of which I understand the Law Council bankruptcy committee is a member?

Mr Lhuede—No, we have not because, firstly, the bill was released in, I think, early December and the forum has not met since then; and, secondly, with December being a very busy period and everyone disappearing at Christmas time, there has been no opportunity to raise those technical issues.

CHAIR—We do understand that problem. We have of course been dealing with this across the same period. We can pursue those matters. Are you the Law Council's representative on the Bankruptcy Reform Consultative Forum?

Mr Lhuede—Yes.

CHAIR—How would you characterise that consultation process?

Mr Lhuede—The forum, I think, works very well. I am very proactive in congratulating the inspector-general on the better consultation that has gone on since its inception than what happened beforehand. It is nice to see that the system works insofar as regard has been given to the submissions which have been put through the Law Council and there has been reaction at the legislative level in line with the submissions from time to time. Of course there are policy issues, and we do not necessarily agree with what has been put, but I can certainly say from our perspective that we are very pleased to see that the forum does exist and, as far as we concerned, it does work. The superannuation bankruptcy issue is an example of that. I am not sure if it was a formal forum session but it was certainly convened out of that. There was wide consultation on the earlier proposed changes to the bill, and I had been quite forceful in my views about how we should change it and, equally, that I did not like the earlier proposal. There might be self-interest in that but it was basically going to double the size of the bankruptcy legislation if they had persisted with those changes. It would have added huge complexity to bankruptcy.

Bankruptcy in superannuation is a relatively small issue. It is very important that we do close off these loopholes but, at the end of the day, there are only a handful of cases that have come to the fore. That is not to say that it does not happen and go unnoticed, but I practise extensively in the area and I certainly do not see a hell of a lot of it. So it is very pleasing to see that there has been a measured response to what has been identified as a significant problem.

CHAIR—Finally, given the very comprehensive submission that you have made in your other capacity, would you like to draw the committee's attention to any particular matters in that submission?

Mr Lhuede—No, not really. The latter problem that is identified in the Law Council submission is probably the remaining problem. If we had persisted with the initial proposal for reform relating to the superannuation problem then we would essentially have been readdressing the public policy issue of whether or not superannuation is to be protected and, if so, to what level. Regarding the manner in which this bill proposes to fix the problem, we are simply restating the well-established public policy position of protecting superannuation up to a given threshold level.

I suppose one thing that arose out of the budgetary announcements that relate to superannuation changes is that I have been persistently asked, 'What is the government going to do about the threshold levels?' Of course, going forward, at some stage there will be contributions of up to $50,000, but the reasonable benefit limits will essentially be abolished, as I understand it. Now, if that is the case, what is to become of the reference to reasonable benefit limits in section 116(2)(d) and the protection afforded under that? At the moment, superannuation is protected upon bankruptcy up to the reasonable benefit limit, which is about $1.3 million; anything over and above that would be available to creditors.

An issue I raised in my submission was whether the concept of reasonable benefit limits is extended out of the original amendments. I think there is provision for a deemed increase in limits where people held significant superannuation assets upon the introduction of the Superannuation Industry (Supervision) Act 1993. I have had the question—I have had to consider it once before, and I cannot remember the expression, although I can refer to my paper if you like. The present provision is for a limit of $1.3 million, but will the deemed limit increase for people who held significant moneys back upon the introduction in 1993 of the Superannuation Industry (Supervision) Act carry across to the Bankruptcy Act? So if someone had, say, $5 million or $6 million in super back in 1993, will that limit carry through and be defined as a 'reasonable benefit limit'?

It is a technical argument. My view from a legal perspective is: no, it does not, and it is a reasonable benefit limit. But I have actually had cause to consider that in the past, and I am aware of at least one former colleague who disagrees with me in that regard. So, in terms of protection thresholds, you might look at that, but I suspect that, with the changes generally, reasonable benefit limits as the threshold will be altered and they will either adopt it and index it going forward, under the Bankruptcy Act, or they will put in a new system. But generally I think a threshold level is appropriate there. As it stands, I do not think there is too much objection to the existing levels.

CHAIR—Thanks, Mr Lhuede. We may find ourselves here discussing that again on another occasion. Further questions?

Mr Lhuede—The reference was to 'transitional reasonable benefit limits'; that was the expression I was looking for.

CHAIR—Thank you. We might start with Senator Mason.

Senator MASON—I have one question. It relates to the concern you raised, Mr Lhuede, on page 3 of your submission, the Law Council's submission—the second point. How would you overcome that problem? I understand the policy point that you are making, that general superannuation should be protected from bankruptcy proceedings, but how do we overcome that problem?

Mr Lhuede—There is provision for that in the act now. It is section 116(2)(g), dealing with proceeds from personal injury claims. A person who has a personal injury prior to bankruptcy receives a fund of money, and that money is protected notwithstanding when the money comes into existence—whether it be pre or post bankruptcy. And there is already a mechanism in the act to deal with that. It is section 116(2)(m) or thereabouts.

Senator MASON—So the principle has been established of, in a sense, quarantining money from that exercise?

Mr Lhuede—Yes. Basically, if you have a fund of money pre-bankruptcy—and personal injury is a good example, where you might end up quadriplegic and have to buy a special home—you quarantine the money. What the act does is quarantine the fund so that, if the fund is converted into assets which are extant and can be identified, then the protection extends to those assets you can trace. Superannuation is an interesting one. I have been putting this forward for some time as an issue and waiting to see if there is some policy reason why we do not extend it to super funds pre-bankruptcy. I suppose there is one example of a situation where you might say you ought not be protecting moneys coming out of superannuation funds pre-bankruptcy, and that is where there are early withdrawals.

Senator MASON—Do you mean out of character early withdrawals?

Mr Lhuede—Yes.

Senator LUDWIG—You would have to have a main purpose.

Mr Lhuede—There is provision under the act. Under the superannuation legislation there are hardship provisions. I think APRA has the say-so. You can apply to APRA for the release of funds. For the hardship provisions, principally you have to show that your house is going to go. From a general policy perspective I have a real problem with saying that people can pull funds out and put them into saving the house when they then go bankrupt. It is in that very situation that you probably should not be taking moneys out of super—if they are in a financial hardship situation—because they are about to go bankrupt.

Senator MASON—Yes, and they are protected in superannuation.

Mr Lhuede—Yes. I think there is a real case for saying that those sorts of withdrawals should be protected. Of course then there is the other situation, where a person is retired and it turns out that the guarantees which he gave five or 10 years ago have been called in, his superannuation moneys are vested and he then goes bankrupt. The underlying public policy is that we do not want to throw superannuants on the welfare system, but that is exactly what will happen, having vested that money in the individual who has then gone bankrupt: they are going to lose the lot.

Senator MASON—Thank you for your assistance.

Senator LUDWIG—The only area that seems to stand out a little bit—and you do not really comment on it in your submission, and I might ask you why—is the rural support grants. Why would they have special treatment? Should they have special treatment? Have you turned your mind to that? Is there a class of things that should have special treatment?

Mr Lhuede—We have not commented on it. When the executive sees fit to grant money to classes of individuals, these payments are generally made in hardship cases, to buy them off the land et cetera. Why would the government be giving money to individuals for that to then go to their creditors? The moneys are given for specific purposes, either in hardship cases, to try to help them onto their feet—where presumably the money is to be applied in certain ways: grants for assistance on the farm et cetera—or, alternatively, if you look at the dairy adjustment scheme, to buy people off the farm. If that is to happen, then essentially it is a

government grant. I do not see a problem with the government saying that they will allow some financial consideration in those circumstances but they do not necessarily just want it going into the mix to go to the general body of creditors. If they want to do that, well and good. I am sure that trustees and Mr Cook would welcome that because it would be going to the general body. But it may not be going to meet the government's objectives for which the moneys were originally granted.

Senator LUDWIG—By analogy, then, wouldn't it also apply to other grants made outside of the rural area to businesses? There is a range of grants, as you can imagine, made by state and federal governments to support business, either directly or indirectly. Wouldn't the same, by analogy, apply? I not asking you that—I will ask the government—but it would seem that if that principal, which you say is sound, applies, then it would also apply to those others as well.

Mr Lhuede—Logically, yes. I suppose there is a practical issue, that the money gets put in and used up in the mix. I am not too sure how the rural grants scheme is going to work and what the underlying criteria are. If it is a case of the money just sitting in the recipient's bank account for a period and they then go bankrupt, then that fund of money in the ordinary course will be available. The reality is that these moneys are going to be used, one presumes, to meet ongoing expenditure; it is not going to be around long. Trustees cannot drag it back once it has been spent, unless it has been spent to acquire the Mercedes, the share portfolio or something to that effect. But that is not really what the moneys are for.

Senator LUDWIG—I will take the opportunity to ask the Attorney-General. Thank you very much.

Senator TROOD—I want to ask you something, Mr Lhuede. I think you were here when I was having the discussion with Mr Cook about trying to provide a little more certainty. Do you have any views on that that might assist the committee?

Mr Lhuede—The public had this debate as recently as 1996 when there was the reform of sections 120 and 121 of the act. I see nothing wrong with the current legislation in section 121. I am disappointed to see that it is not applied more often. I do not think it ought to be as hard as people make out to bring these cases. Clauses 128B and 128C are essentially a rewriting of section 121. There is not a lot of difference between them. The significant difference is the one to cure the problem of superannuation. I am loath to start bringing in examples. As a lawyer, I do not think it makes for good legislation. People tend to get tied down by that and courts tend to start interpreting from those examples.

The fact is that we have a body of case law still developing on section 121. It is interesting to look at the number of bankruptcy cases that have gone to the highest court in Australia in recent times. I can give you three names from recent times of High Court cases on bankruptcy. We have not ever had so much judicial consideration of the Bankruptcy Act at that level. There was the Cummins case last year, there was Peldan v Anderson just before Christmas on a very particular provision of section 121 and, of course, there was the Cook v Benson case. There is a body of case law; it does work. The provision of 121(2) is a deeming provision which says that, if they are insolvent at the time of the transfer, the individual is to be taken to be insolvent. It is not a rebuttable presumption. The evil we are trying to address

in 121 is people giving away property at times when they are insolvent. There is nothing wrong with people giving away their property but, when they are insolvent, we as a community say that that is inappropriate. That is what that section addresses; clauses 128B and 128C simply reflect that.

The question you put to Mr Cook was: do we need to start defining the criteria? Courts can work it out, but the primary test of a trustee is not going to be those criteria. I think Mr Cook said that if you see the elephant in the room you can usually identify it. You can. The courts can and do. The primary question is one of proof of intent. You probably do not even need that section in there because there are a series of cases already on the books which say that the courts are to have regard to the surrounding circumstances in proof of intent. But you do not even need to go there if you can prove the person is insolvent. That is probably the primary means by which trustees will run a 121 case. Similarly, they will now run a 128B case.

Senator TROOD—Eloquent support for the common law, Mr Lhuede.

Mr Lhuede—Yes. The courts do work as a rule—not always, but usually.

CHAIR—There have been some inconsistencies between our witnesses on that point! May I thank you, Mr Lhuede, for your time today and for attending the committee—it is very helpful to us—and for the submission you have provided on behalf of the Law Council and for the separate submission you have provided on your own behalf. Thank you for your assistance.

Mr Lhuede—Thank you.

[10.46 am]

COLES, Mr Tony, Manager, Superannuation, Retirement and Savings Division, Department of the Treasury

GLENN, Mr Richard Alexander, Acting Assistant Secretary, Office of Legal Services Coordination, Attorney-General's Department

BERGMAN, Mr David, Adviser, Policy and Legislation, Insolvency and Trustee Service Australia

GALLAGHER, Mr Terry, Chief Executive and Inspector-General in Bankruptcy, Insolvency and Trustee Service Australia

CHAIR—I welcome the witnesses from the Insolvency and Trustee Service Australia, the Attorney-General's Department and the Department of the Treasury. I remind senators that the Senate has resolved that an officer of a department of the Commonwealth or of a state shall not be asked to give opinions on matters of policy and shall be given a reasonable opportunity to refer questions asked of the officer to superior officers or to a minister. This resolution prohibits only questions asking for opinions on matters of policy and does not preclude questions asking for explanations of policies or factual questions about when and how policies were adopted. Officers of departments are also reminded that any claim that it would be contrary to the public interest to answer a question must be made by a minister and should be accompanied by a statement setting out the basis for the claim. Are there any opening statements?

Mr Gallagher—Yes. The primary purpose of the Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006 is to allow bankruptcy trustees to recover superannuation contributions made prior to bankruptcy with the intention of defeating creditors. The amendments address a very significant threat to the integrity of the bankruptcy system by ensuring that a person cannot, in anticipation of bankruptcy, convert assets into superannuation to avoid paying their debts.

The amendments are proposed in response to the High Court's decision in Cook v Benson in June 2003. That case concerned section 120 of the Bankruptcy Act, which allows a bankruptcy trustee to recover property transferred by the debtor in the lead-up to bankruptcy where the debtor received inadequate consideration for the transfer. In Cook and Benson, the trustee was attempting to recover superannuation contributions made prior to bankruptcy on the basis that the trustee of the superannuation fund had not provided 'valuable consideration'. The High Court decided that the superannuation fund trustee had provided valuable consideration in the form of a promise to manage the money properly and ultimately pay retirement benefits to the bankrupt.

The case concerned section 120 as it existed prior to 1996. Instead of referring to 'valuable consideration', section 120 now provides that a transfer is void where the transferee gave no consideration or gave consideration of less value than the market value of the property transferred. However, the same issues apply to the current version of section 120 and also in relation to section 121, which provides for the recovery of property transferred prior to

bankruptcy with the intention of defeating creditors. This is a very significant loophole because it means that a person contemplating bankruptcy can deliberately convert existing assets into superannuation to defeat creditors, leaving the bankruptcy trustee and the creditors with no recourse to those assets.

The amendments have been developed following extensive public consultation, which has lasted more than three years. Much of the difficulty in finalising the amendments arose from earlier proposals to allow bankruptcy trustees to recover 'excessive' contributions made in the five-year period prior to the bankruptcy. These proposals were an attempt to find an appropriate balance between the need to protect creditors on the one hand and the need to encourage retirement savings on the other. These earlier proposals were strongly criticised, with much of the criticism being related to conflicting ideas about determining what contributions should be treated as 'excessive'. The proposals were also criticised because of complexity they could have added to both bankruptcy and superannuation systems. The government decided in 2005 to abandon these proposals and focus instead on contributions that have been made deliberately to avoid paying creditors. That decision also takes account of the government's announcements in relation to simplifying superannuation. Complex provisions in the Bankruptcy Act could have undermined that aim.

The amendments will provide that a contribution made by the bankrupt to an eligible superannuation plan with the intention to defeat creditors is void against the trustee and bankruptcy. This is based on the existing section 121. The amendments will also allow the trustee to recover contributions made by a person other than the bankrupt for the benefit of the bankrupt where the bankrupt's main purpose in participating in the arrangement was to defeat creditors. For example, this will cover contributions made by the bankrupt's employer where the bankrupt has entered into a salary sacrifice arrangement to defeat creditors. The amendments will ensure that, in relation to contributions made to defeat creditors, any consideration given by the superannuation fund will be ignored in determining whether the contribution is recoverable by the trustee. This will overcome the effect of the decision in Cook v Benson.

It can be difficult for a bankruptcy trustee to prove the bankrupt's intention at the time of making a transfer. Section 121 deems this to have occurred where the bankrupt was insolvent at the time of making the transfer. The amendments include an equivalent provision in relation to superannuation contributions. In addition, the court will be able to take into account the bankrupt's historical pattern of contributions in determining whether the required intention existed. The fact that the contributions were out of character, given the bankrupt's history, does not give rise to any presumption that they were made to defeat creditors; the amendments merely direct the court to take this into account.

The amendments will clearly protect a superannuation fund from any liabilities for fees, charges and taxes it has paid in relation to the contributions. This is important, as the superannuation fund should not be liable for money that it has properly paid under tax or superannuation laws or pursuant to the rules under which it operates. The amendments will also explicitly provide that, where the superannuation fund repays contributions which are void against a bankruptcy trustee, it is not exposed to any civil or criminal liability in relation to that payment.

The act already contains provisions which allow the official receiver to issue notice for the recovery of property which has been transferred prior to bankruptcy in contravention of sections 120 and 121. This bill will include similar provisions allowing the official receiver to recover void superannuation contributions. The amendments will also allow the official receiver to issue a notice to the superannuation fund to freeze the member's interest in that fund while recovery action is under way. This will prevent the bankrupt from withdrawing or transferring those funds in circumstances in which the bankruptcy trustee is entitled to recover them.

Our consultation with industry stakeholders from both the superannuation and insolvency sectors has revealed broad support for this approach. The amendments are largely designed to have a deterrent effect by putting people on notice that contributions made to defeat creditors will be recoverable in the event of bankruptcy. We would expect the provisions to be used rarely, on the basis that people will be advised that superannuation contributions may be an ineffective means of protecting wealth when bankruptcy is approaching.

The bill also includes amendments which will streamline the provisions relating to protection of certain types of rural grants in the event of bankruptcy. These are payments made as part of restructuring parts of the rural sector. The amendments represent no change to current bankruptcy policy. The act already protects payments made under the dairy exit scheme and the Rural Adjustment Scheme, by providing specific exemptions under section 116. However, other similar payments, such as those under the Sugar Industry Reform Program and the tobacco growers adjustment assistance package, are not protected. It is cumbersome to require amendments to the act when these schemes are established, particularly as they are often established administratively. The amendments in this bill will allow categories of payments to be prescribed by regulation, which will ensure payments can be protected more quickly without the need to pass legislation.

Finally, the bill makes some minor technical corrections to the act. In particular, they will correct an error in an amendment made last year to section 121 by the Bankruptcy Legislation Amendment (Anti-avoidance) Bill 2006 and remove inappropriate references to the official trustee in the Proceeds of Crime Act 2002 which imply that the official trustee has responsibility for handling public money. The amendments will clarify that it is the Inspector-General who performs this role.

CHAIR—Thank you. Mr Coles, do you wish to add anything?

Mr Coles—I have nothing to add to the opening statement but I will make a brief comment based principally on listening to the hearing today and reading the submissions. From a broader policy perspective we seem to have almost got it right. There are a number of competing policy principles involved in drafting this law, from the protection of retirement income and superannuation moneys to protecting the rights of creditors. Both are legitimate and both are important. From a legislative perspective and a policy perspective we need to deal with complexity and simplicity in the law—how we deal with the problem. Everyone seems to think that we have got it right, but there are certain complaints about how we have done it. Not everyone is happy. Neither side is happy in respect of certain minor policy matters. I think that probably means that from a policy perspective we are generally on track

to getting it right. We cannot satisfy everyone. Overall it is not a bad piece of legislation for what it is doing.

CHAIR—Thank you. You sound almost quizzical about that, Mr Coles—as if it has come to you as some surprise.

Mr Coles—It is unusual; this is my first appearance before this particular committee.

CHAIR—We are grateful for your observation and your presence here today. I will begin, Mr Gallagher, by saying that it is often the habit of this committee to complain loud and long about lack of consultation involved in legislation that is presented to us, but I can say with some confidence both in relation to the submissions and the appearances of witnesses today that it does seem to have been a very constructive process, and the committee is very glad to see that. It does make our job considerably easier. As Mr Coles adverts to, there are matters of a minor technical nature and a minor policy nature, some of which have been put to you and some of which have yet to be. Particularly in relation to those matters raised by witnesses who have appeared here today, the committee would be grateful for some brief responses from you, as far as you are able, to assist us in the preparation of our report.

Mr Gallagher—Yes. Thank you.

CHAIR—We will move to questions.

Senator LUDWIG—Was this bill drafted prior to the rules for simplified super? If so, do you foresee any amendment to the bill to take into account the new simplified super rules? I note one of the submissions indicates that with the removal of the RBL there should now be a $1.4 million limit in terms of a new RBL limit for this legislation. Do you see any need for that? There are a couple of questions there that I thought I would give you a broader opportunity to answer.

Mr Gallagher—I will endeavour to answer the first question and leave Mr Coles to partly answer the second. The bill was drafted in the knowledge of the change to superannuation arrangements announced in last year's budget. So, whilst the first discussion paper, which is the one that was roundly criticised, was pre those announcements, we already had received the comments about those by the time the superannuation announcements had been made. So they were able to be taken into account.

Mr Coles—In respect of the application of the removal of the pension reasonable benefit limit—I think it is in section 116 of the Bankruptcy Act—there has not been any formal government announcement as to which way they are going, so there is not much I can actually add to that, apart from saying that the government are aware of the issue, are considering it and will respond in due course.

Senator LUDWIG—What will that mean for this bill, though? I accept that you have taken the issue on board, but will it have an impact on this bill? Will there now be a requirement for a later amendment should the government decide on a policy? I guess it is a little hypothetical too.

Mr Coles—It is a little hypothetical, and I cannot really provide any further guidance in respect of that because the government have not made a decision. But there is a significant bill currently before the parliament to do with the simplification of superannuation measures.

The government have announced that there will be consequential bill which will be considered cognately in the Senate's review of the Tax Laws Amendment (Simplified Superannuation) Bill, so there is an opportunity for legislative amendments if required.

Senator LUDWIG—Thank you. I do not know that I can explore that any further in this way. Does the bill purport to cover self-managed superannuation funds?

Mr Coles—Yes. Basically, it deals with any contribution from a superannuation fund presumably regulated under the Superannuation Industry (Supervision) Act. That includes trustees who are self-managed superannuation funds.

Senator LUDWIG—Is there a class of superannuation funds that, if they fail to register or are not regulated, would fall outside this legislation?

Mr Coles—Generally we find that most superannuation funds come under the SI(S) or Superannuation Industry (Supervision) Act simply because they get the tax advantages of the reduced tax rates that apply under it. There are non-complying funds, funds that do not comply with the SI(S) Act. These entities do exist, but they are generally not involved—and they are pretty much trusts, so I expect that they would be dealt with under the normal provisions of the Bankruptcy Act.

Senator LUDWIG—That was the question I was going to go to. Thanks for elucidating that for me. Does ITSA believe the existing legislation is adequate for dealing with those non-complying funds, or will this new legislation apply?

Mr Bergman—There are provisions in the Bankruptcy Act at the moment which may apply, but it is difficult to respond determinedly to that without a specific, factual situation.

Senator LUDWIG—Well, a non-complying fund.

Mr Bergman—But what would the transfers be—what would the transactions be that we would be looking at? Just a—

Senator LUDWIG—A payment.

Mr Bergman—contribution into a fund?

Senator LUDWIG—A one-off contribution of a significant amount after the simplified super legislation comes into place, one that amounts to a transfer.

Mr Bergman—There may be scope to recover that under the provisions in division 4A of part VI, which is about transfer—

Senator LUDWIG—I wonder if you take that on notice and have a look at it.

Mr Bergman—Yes, we would be happy to do that.

Senator LUDWIG—Because what we may have now seized upon is an area where there is potentially a gap. The intention is to cover superannuation funds; the intention is to close a loophole. And I am sure you would join us in wanting to close the entire loophole across superannuation funds. There are, unfortunately, superannuation funds that do not comply. They are still quite legitimate, they exist and they are out there, but they are not covered by the SI(S) Act, in which case they may not come within this area. Will they be picked up under the bill we are considering or will they be picked up under existing legislation? And will the

same rule apply—in other words, the rule set out in this bill to determine whether or not the trustee can pursue them? That is, to use the phrase in the bill, where there is an 'intention to defeat creditors' with a one-off payment. Will the same rule apply, or will you apply different criteria? And, if that is the case, could you perhaps explain what those criteria are?

Mr Gallagher—We will certainly take on board that request. The one point that I can make is that section 116, which provides protection to money put into a superannuation fund, is at the heart of this issue. Moneys held in funds that are not approved funds do not have that protection.

Mr Bergman—That is correct.

Senator LUDWIG—Yes, but they are still a non-complying superannuation fund. So, for all intents and purposes, they are a superannuation fund. Mr Coles, correct me if I am wrong but I am sure that you would recognise them as superannuation funds; therefore, one rule would apply to complying superannuation funds, through this bill, and will require those people to have cognisance of that. What I think you are now suggesting, and what I am asking you to have a look at, is that a different rule will apply to non-complying funds, which, for all intents and purposes, are superannuation funds. In my view, it would be consistent to have the same rule apply to both. It is perhaps a policy decision, but at least you could have a look at it.

Mr Bergman—Yes, we will look at it.

Senator LUDWIG—Thank you. Mr Gallagher, I take it that you have had an opportunity to have a look through the submissions made to the committee. A number of technical issues have arisen, and I am not sure whether I should deal with them individually.

CHAIR—Excuse me, Senator Ludwig, I am not sure whether you are aware that I have asked Mr Gallagher and Mr Bergman to take on notice those technical issues on matters of policy which have been raised in some of those submissions and to respond briefly to the committee.

Senator LUDWIG—Terrific—that saves me trying to sort through them.

Mr Gallagher—We received a number of submissions late yesterday and we received some submissions earlier. We have endeavoured to put our minds to some of those issues.

CHAIR—The secretariat will provide you with the questions.

Mr Gallagher—We will not necessarily have a comprehensive response to them, but if your questions are about those we are happy to try to answer them.

CHAIR—In the normal of course of events, Mr Gallagher, we would extract those and provide them to you as questions.

Senator LUDWIG—I have ticked a few questions through the submissions. I will pass them to you through the secretariat so that you can respond so that we have something concrete to deal with. If there are any for you, Mr Coles, the secretariat will do the same.

Mr Coles—Yes.

Senator LUDWIG—I am not sure whom I should ask about where the request for the exemption for rural grants came from. I can understand in part the policy, and I am sure you were in the room when I asked this question of the Law Council. I understand that point, but

why that area? Why not the Regional Partnerships grants, which are also in that area and which, I suspect, are provided for similar purposes? Why was it just the rural grants area and where did the request come from?

Mr Gallagher—May I say firstly that, in this part of the amendment, there is no change to the bankruptcy legislation in the sense that these protections already exist. The problem arises when new schemes of assistance come up, because sometimes it is cumbersome to incorporate them or to consider whether they should be protected under bankruptcy legislation and to incorporate them at the time.

So the suggested change here is not an alteration to a policy but a mechanism to facilitate that to occur. But, as far as your question concerns why this kind of assistance and why not other kinds of assistance, that is a policy decision. I do not think there is anything more I can say about that. It was a decision taken at the time that those grants were being made.

Senator LUDWIG—Does the request for the inclusion of that exemption come from ITSA or from A-G's?

Mr Gallagher—The inclusion of additional forms of assistance arose out of the issue coming to light in the context of recent forms of assistance where the anomaly was exposed.

Senator LUDWIG—What about regional partnership grants? We have now exposed that one, so why would that not be exempt? It is money from government, it is directed to rural areas and it is for a range of purposes.

Senator TROOD—Perhaps the answer lies in the fact that the grants to which Mr Gallagher was referring are largely grants to individuals and reflect income, whereas regional partnership grants are largely to institutions, clubs and associations. I am speculating on that subject, of course.

Senator LUDWIG—Yes, I know. I considered that as well, because they are grants to individuals. Are they grants to pastoral companies or to individuals of pastoral companies? I am not sure. Perhaps Mr Gallagher could tell me whether they are grants to individuals or pastoral companies as such.

Mr Gallagher—I am not aware.

Senator LUDWIG—Then where could I find out? The committee is limited in the people before it. I am sure Mr Coles cannot help me. How do I determine why rural grants of that nature are exempt? What are they? I'll have to ask the A-G what the policy regime was. Once we determine the nature of that grant, why particularly that grant and not others?

CHAIR—Would you like to place the question on notice, Senator Ludwig?

Senator LUDWIG—It might be the only way we can deal with it.

CHAIR—That can then be sent through the appropriate channels for a response.

Senator LUDWIG—All right. Can I consider that done?

CHAIR—You can consider that done, yes.

Senator LUDWIG—Thank you. I might pause there to allow others to have an opportunity to ask questions.

Senator TROOD—I have a question about the rural support, but it is a technical one about the way in which this is now going to take place in reference to your observations, Mr Gallagher. I gather that, rather than there being a need for legislation in relation to particular schemes as they may come in from time to time, they are going to be now handled by way of regulation so that they can be more easily added to the range of schemes which fall within the provisions of the act. Is that right?

Mr Gallagher—Correct.

Senator TROOD—The only other question relates to your allusion in your opening remarks to the motivation for the legislation. How widespread a problem is this that we are dealing with?

Mr Gallagher—As has been commented on by previous witnesses, there is not a high volume of instances of which we are aware. Certainly a large number have not been litigated where this has arisen. The need for the legislation arose from the particular decision in Cook v Benson where the court's decision exposed a major loophole because it effectively said that consideration was provided by the superannuation fund by promising to pay the money back to the person when they retire. It simply exposed a loophole that said, 'That is the law, therefore people are perfectly entitled to offload their assets before they go bankrupt', and the superannuation fund was providing consideration. I guess the urgency and the concern is about the potential that was created by the decision rather than the high incidence or frequency of the problem.

Senator TROOD—It is an interesting definition of 'urgency': the legislation was introduced in 2006 and the High Court decision was in 2003, as I understand it.

Mr Gallagher—I think the time frame is a reflection of the complexity issues that arose.

Senator LUDWIG—There has been a request for a delay of implementation by a number of submitters as well. I want to explore on record with you the view of ITSA on what requirements there might be for superannuation funds to comply with the legislation, how onerous it would be, what sort of impost might it be on their record keeping, whether or not it is your understanding that they already keep those records and it is just a matter of extracting that data and providing it to the relevant creditor, as the case may be, and what you think the scale of that demand might be.

Mr Gallagher—I will provide an answer and I will also invite Mr Bergman, who is more heavily involved in the consultations on this. There will be a requirement in the official receiver notice for the official receiver to document the nature of the payment, and certainly before the official receiver issues that notice he or she would need to be satisfied as to the evidence supporting the claim. So I think it is drafted and the intention is that the onus is on the bankruptcy trustee, through the official receiver notice, to provide the evidence in support of the claim for the payment.

Mr Bergman—The only obligation on the super fund is to pay the money, ultimately. I guess it is firstly to establish that it has the money—that the member's withdrawal benefit covers what is being claimed—and then to pay the money. There also may be requests for information, but we are talking about a very small number of cases. The provisions are largely

about deterring people from doing this in the first place, so we would expect that the actual recovery process would not occur in more than a handful of cases.

Senator LUDWIG—So the workload is really placed upon the official trustee. Once the official trustee has collected the relevant information, the request is made to the super fund and usually the official trustee, at that point, would have to satisfy the superannuation fund that it is a request and that it provided sufficient detail to the superannuation fund to meet it.

Mr Bergman—That is right. It is the official receiver who makes the decision, who has to be satisfied and who gives the notice to the super fund. The super fund trustee does not then have to make another decision other than if the money is actually there for them to pay out that day. The other thing that I would say about what it means for super funds is that it does depend to a small extent, perhaps, on the response to some of these other technical issues that they have raised in relation to how they might comply with the notices.

Senator LUDWIG—Yes, with freezing notices and the like they may need to have a system in place to ensure that those notices are acted upon and the funds frozen.

Mr Bergman—For example, one of the issues that were raised in a few of the submissions was how the refund of fees, charges and taxes that are paid are dealt with. That will have an impact on what the super fund has to do, depending on whether the bankruptcy trustee does it or the super fund trustee does it. The other thing is that we have, in the course of consulting with the super industry on this, been very cognisant of the implementation issues. They have taken the opportunity to raise those with us early. But there is a bit of a trade-off between reducing the complexity that would have been apparent from earlier proposals and having a system which is more limited in its application and does not introduce great complexity for the super funds to have to administer it. We have spoken to them about things like the way that they could build on systems they already have in place to make payments for other purposes. Depending on the final form of this legislation when it is enacted, we would more than happy to be talking to them further about those implementation issues. The examples that were given this morning about things like what the notices will look like, how they will recognise them and how they will know exactly how to comply with them are all issues that we can deal with—

Senator LUDWIG—Relatively quickly and easily?

Mr Bergman—Relatively quickly.

Senator LUDWIG—So you do not particularly see a need to extend the implementation date on the basis that has been advanced by a range of submitters that it would create an impost on their recordkeeping requirements?

Mr Bergman—No.

Senator LUDWIG—In terms of the number, do you keep statistical data on how many we are talking about? I know we have kicked this football around a little bit, but I am trying to get an understanding of the scale and the nature of the amounts that are involved.

Mr Gallagher—I think I mentioned earlier that the number of cases that have been litigated is very few. If there have been instances prior to the Cook and Benson decision, where a trustee sought to recover from a superannuation fund and through negotiation that

payment was made or was not in dispute, we do not have that information. We do not really have the mechanism or the wherewithal to collect that. It would just be part of a normal administration of a bankruptcy.

Senator LUDWIG—I thought it would be difficult. There may have been a notification requirement, but if there has not been then it may have been by agreement that that was resolved. If so, only where it has been litigated obviously it has stepped up to the—

Mr Gallagher—I should acknowledge that the official trustee is also a trustee and it does administer a number of bankruptcies. I cannot quote numbers but there were very few instances of this occurring.

Senator LUDWIG—Thank you.

CHAIR—I am not sure that there are any further questions, Mr Glenn. Due to the ruthless efficiency of the committee and the particularly helpful nature of our witnesses today, we are running a little ahead of time, as I am sure you are aware, but we would like to thank you for joining us.

Mr Glenn—Thank you for having us.

CHAIR—I do not know whether there are any particular comments you wish to make, but one matter which Senator Ludwig has been pursuing is in relation to the genesis of the rural packages component of the legislation. I do not know whether your department has had any involvement in that.

Mr Glenn—We have had involvement in the sense of providing oversight for ITSA's work. I am not sure that we have had any other more direct work in the genesis of that policy. Mr Bergman might correct me, if I am wrong.

CHAIR—No, and we have undertaken to place a question on notice to provide the committee with further information. Thank you for that clarification. As there is nothing further, may I thank all of the officers for appearing today and for your assistance to the committee. There are a number of matters, Mr Gallagher, which you in particular, on behalf of ITSA, will receive as questions on notice. As you know, we have a reasonably tight turnaround, so the committee would be grateful for your assistance in obtaining responses to those questions.

Mr Gallagher—Certainly, Senator.

CHAIR—Thank you for appearing and I thank all other witness who have given evidence to the committee today. I declare this meeting of the Standing Committee on Legal and Constitutional Affairs adjourned.

Committee adjourned at 11.22 am