BRI Ferrier

INDUSTRY INSIGHTS

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Insolvency law reforms and the implications for Australian business

Two new sets of insolvency law reforms will be instituted in Australia over the next couple of years:

1. The Insolvency Law Reform Act 2016
2. Proposed reforms outlined in the National Innovation & Science Agenda (NISA) 'Improving bankruptcy and insolvency laws' proposals paper.

The Insolvency Law Reform Act 2016

The first set of laws are contained in the Insolvency Law Reform Act 2016, anticipated to commence in March 2017.

The changes incorporated by the Insolvency Law Reform Act 2016 are relatively simplistic, and are frankly, window dressing compared to the wholesale reforms contained in the NISA proposal.

The laws amend some administrative functions in the insolvency industry. They increase the powers of ASIC to regulate corporate insolvency and aim to improve confidence in the insolvency profession.

The Act focuses on the registration of insolvency professionals, insurance, discipline, referrals involving the Australian Restructuring, Insolvency & Turnaround Association (ARITA) and practitioners, and the prohibition of improper benefits.

It also improves the position of creditors, in terms of their powers of removal, requests for information, reviews of estate or external administration, and directions.

Overall, however, the laws will make little difference to the Australian insolvency regime. While they may streamline the insolvency industry a little, and commoditise the industry to an extent, they will not have a major impact on how business insolvencies in Australia are addressed.

The NISA proposed reforms

Of greater significance are the reforms proposed proposed by the Australian Government's National Innovation & Science Agenda.

The NISA proposals paper, issued in April 2016, outlines three key measures:

1. reducing the current default bankruptcy period from three years to one year
2. introducing a 'safe harbour' for directors from personal liability for insolvent trading if they appoint a restructuring adviser to develop a turnaround plan for the company

3. making 'ipso facto' clauses, which allow contracts to be terminated solely due to an insolvency event, unenforceable if a company is undertaking a restructure.

The Government's submissions process – enabling interested stakeholders to provide feedback on the proposals paper – closed on 27 May 2016.

Implications of the proposed reforms

The ultimate objectives of the NISA proposed reforms are to encourage entrepreneurship in Australia, protect creditors and generate business growth.

Some commentators have suggested they may 'incentivise' bankruptcy, with the numbers of people filing for bankruptcy each year likely to skyrocket.

We believe, however, that these suggestions are over-stated and that, even if a small rise in consumer-related bankruptcies occurs, this uptick should be outweighed by the benefits generated through increased entrepreneurial activity.

Although not every new business opportunity will thrive, these reforms should encourage more businesses to take calculated risks and hopefully succeed. This, in turn, will help grow the economy and will benefit the nation as a whole.

Preserving value

The changes focus on restructuring businesses, improving their prospects for survival and preserving value. If successful, this is a positive outcome for all stakeholders, including customers, employees, shareholders and creditors.

Of course, only viable businesses with competent management teams that are open to change and have the support of key stakeholders are capable of being saved.

The proposed reforms will enable a board of directors, where a business is distressed, to take steps to ensure it doesn't go down the path of a formal insolvency appointment, where value destruction is generally perceived to occur.

The law will give the directors the necessary breathing space to understand what actions the business needs to take to preserve value, without penalty of trading a company while insolvent. Importantly, these reforms aim to provide the directors with protection from claims whilst they explore the available recovery options.

Transparency of restructuring efforts

While insufficient details are currently available as to how this might work, in a practical sense, there is likely to be an obligation on the part of boards to inform creditors that the business is financially distressed, and that they are reviewing operations and are acting to improve the situation.

The directors will likely be required to make this information public before renegotiating with customers and suppliers. This should encourage belief in the somewhat transparent process in the hopes of garnering the support of key stakeholders.

Encouraging directors to act early

The reforms should encourage businesses to act much earlier, when facing financial distress, than is often currently the case.

In the existing regime, evidence shows that many directors, when business faces financial distress, are first concerned for their personal, professional reputations. In this situation, where they don't have legal protection, rather than exploring the turnaround options available and be exposed to trading losses and insolvency, they might simply resign.

As a consequence, the best people available to effect a turnaround are no longer available. In such cases, a formal insolvency appointment is the only viable option to preserve the remaining value for creditors.

The proposed reforms will create a 'safe harbour' where directors are protected and are given time to explore options for restructuring the business and hopefully avoid a formal insolvency appointment.

The 'restructuring adviser'

The proposed reforms centre on the appointment of a 'restructuring adviser' to lead the proposed turnaround activity.

A major question that remains to be answered, therefore, is the type of professional this adviser is likely to be.

The success of a business restructure is contingent upon

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a competent professional giving a view as to whether the company is 'capable' of being saved based on its financial circumstances. This ensures that time and effort are not wasted on businesses that are lost causes.

The NISA proposals paper hasn't stipulated who the authorised professional should be. Industry discussion has suggested the individual might come from an insolvency, accounting, banking or legal background.

We certainly don't believe the person in this position should only be an insolvency practitioner. Value may be added by other specialists, so the pool of available professionals should be broader rather than narrower, as long as the ultimate appointees are appropriately qualified.

It has been mooted that the person must have appropriate experience and a track record in successfully rehabilitating distressed businesses back to financial viability. This lends itself to those professionals, such as ourselves, who have historically focused on saving businesses where possible.

Whatever the case, there will need to be an entirely new accreditation regime that reassures all stakeholders, including creditors and other external parties, that someone competent is in the business working to change the way it operates.

About BRI Ferrier

BRI Ferrier is a unique affiliation of expert business recovery, insolvency, forensic accounting and advisory firms. We provide practical, innovative services that help financially distressed businesses to recover or at least minimise the negative impacts of insolvency.

With over 160 staff and eleven practices in Australia, New Zealand, Hong Kong and the United Kingdom, we work with clients of all types – from individuals, sole traders and small businesses to public corporations and government entities.

We also work with financiers, solicitors, accountants and creditors to address the needs of all stakeholders when businesses face financial challenges.

How BRI Ferrier can help

BRI Ferrier can assess your current situation and advise on a path forward to minimise further risk.

Early intervention is often the key for a successful restructure of your business. If you or your client is experiencing financial challenges then don't delay, contact us today.

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The initial consultation to your client is free, strictly confidential and without obligation.

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