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The Federal Government has announced new insolvency reforms that are intended to give businesses more control over how they restructure debts in recovering from the COVID-19 financial downturn.

These reforms are especially important with the temporary protections for directors and companies ending on 31 December 2020, and the Job Keeper subsidy ending on 28 March 2021. The effect of the proposed reforms is to provide businesses that have less than \$1 million in liability, an opportunity to restructure their debts under protections comparable to those afforded under voluntary administration.

### Summary of proposed changes

The changes are inspired by the Chapter 11 Bankruptcy Law in the United States. The key aspects are:

- Businesses with liabilities of less than \$1 million are permitted to stay in control of the business while restructuring their existing debts;
- A small business restructuring practitioner will be retained to assist in restructuring, and in dealing with creditors;
- Once the director/board of directors have approved the appointment of a restructuring practitioner, they are protected from all unsecured creditors, and there is limited protection from secured creditors. These creditors cannot enforce personal guarantees against the directors from this time;
- The business owner has 20 days to develop a restructuring plan, in which time they are still in control of the business; and
- Creditors have 15 days to vote on the restructuring plan, and if accepted the practitioner will oversee the distributions of funds to creditors.

The Federal Government has promoted this mechanism as voluntary administration for small businesses. Many small businesses would not have used the normal voluntary administration process due to the high costs and delays.

### The effect of a re-structuring plan being rejected

If the restructuring plan is rejected, the company will go into a modified version of liquidation. Key changes include:

1. reduced circumstances in which a liquidator can seek to clawback an unfair preference payment from a creditor that is not related to the company;
2. only requiring the liquidator to report to ASIC (under section 533 of the Corporations Act 2001 (Cth)) on potential misconduct where there are reasonable grounds to believe that misconduct has occurred;
3. removing requirements to call creditor meetings and the ability to form committees of inspection;
4. simplifying the dividend process (where creditors receive a return proportionate to their debt) and the proof of debt process (where creditors provide information as to the debt they are owed, which is assessed and accepted or rejected by the liquidator); and
5. maximising technology neutrality in voting and other communications. This includes adopting electronic communication to mitigate time delays, and remove the costs of producing and distributing paper documents.

### Implementation of the reforms

Small businesses are prone to having their assets depleted during the liquidation process through high administrative costs. These changes are intended to provide a form of voluntary administration that small businesses are more likely to use, and in the event the business fails, allow the business owners to walk away with fewer losses.

The proposed reforms have not been introduced to parliament, but the Federal Government is seeking to have the new mechanism in force by 1 January 2021. We will have to wait and see whether this proposed reform sufficiently addresses the concerns of small businesses. We will keep you updated on any developments on this legislation.

If you would like more information on this proposed reforms, or what other restructuring mechanism are available, please contact [Chris Kintis](#) on 02 8235 1251.