Measures to help your business navigate the COVID-19 Crisis

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Various State governments are beginning to formulate plans to wind back the COVID-19 measures which have so greatly affected businesses across Australia. All things going to plan, in the coming months we hope to see an increase in at least some business' ability to generate revenue.

That said, it is expected that it will take time for industries to recover. In addition, there are rumours that the JobKeeper stimulus package may be wound back.

Accordingly, it is important to keep in mind some of the less widely discussed measures the Australian Government has put in place to assist businesses which may still see an appreciable period of time before their revenues return to usual levels.

In particular, on 23 March, the Australian Government introduced two major amendments to the Corporations Act 2001 (Cth). Firstly, new safe harbour measures were implemented to relieve directors from personal liability for insolvent trading – there being an increased risk of this liability arising where revenue of the company's business drops. Secondly, the obligations imposed on companies which have received a statutory demand have been relaxed.

Safe Harbour

The Corporations Act 2001 (Cth) imposes serious consequences on companies and directors for insolvent trading, including that directors of a company can be held personally liable for the conduct of the company.

To moderate the personal risks directors take on in accepting their role as an officer of a company, in 2017 safe harbour provisions were introduced into the Corporations Act 2001 (Cth).

These provisions provide relief to directors who continue to trade when implementing a plan to save the company, despite the company's insolvency. The regime has strict guidelines that must be adhered to and the plan must be thoroughly assessed to ensure it leads to a better outcome.

The Coronavirus Economic Response Package Omnibus Act 2020 (Cth) (COVID Act) amends the Corporations Act 2001 (Cth), by inserting a new s 588GAAA. This temporary section provides a further safe harbour for company directors in relation to their duty to prevent insolvent trading.

Under it, where a company incurs a debt in the ordinary course of business and prior to the appointment of an administrator or liquidator, the directors of that company cannot be found liable for breaching their duty to prevent insolvent trading in relation to that debt. The debt has to have been incurred in the six month period commencing on 25 March 2020.

The Explanatory Memorandum for the COVID Act clarifies that a debt is taken to be in the 'ordinary course of business' if it is a debt that is necessary to facilitate the continuation of the business.

However, this does not necessarily mean business as usual. A director must still comply with its duties to act with 'care and diligence', its fiduciary duties and must still act honestly, without engaging in misleading conduct.

Accordingly, the protections under section 588GAAA do not apply where the business was insolvent prior to the onset of COVID-19, or where the directors are aware that the company will not recover after the crisis has passed.

In such circumstances it would be best to pursue another course of action, such as appointing an administrator to explore options to save the company, or implementing a plan under the original safe harbour provisions. But it is rarely – if ever - black and white, and directors may not know when their company is in a position to repay their debts in 6 months time. As a result, it is very important to gain clarity through proper legal and financial advice.

Statutory demands and bankruptcy proceedings

A statutory demand is a demand for payment that can be made to companies who owe money. Failure to comply with these demands is used as conclusive evidence to show that a company is insolvent.

The Corporations Act 2001 (Cth) imposes time limits within which a company must respond to a statutory demand. This time limit was 21 days. The COVID Act changes the time limit to 6 months, meaning that the debtor company has 6 months to pay the debt, respond to the statutory demand, or apply to set it aside.

Furthermore, the minimum debt amount that can constitute the basis of a statutory demand has been increased from $2,000 to $20,000.

Under the Bankruptcy Act 1966 (Cth), timeframes for an individual to comply with a bankruptcy notice have been increased from 21 days to six months. In addition, the minimum debt for which a creditor can institute involuntary bankruptcy proceedings under the Bankruptcy Act has been increased from $5,000 to $20,000.

These measures are temporary, and unless the government extends them further, they will operate for six months from 25 March 2020.

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