

Tabled
Dated: 14/5/96

**GOVERNMENT
RESPONSE TO
VICTORIAN LAW
REFORM
COMMITTEE'S THREE
"CURBING THE
PHOENIX COMPANY"
REPORTS DATED JUNE
1994 AND MAY AND
NOVEMBER 1995
RESPECTIVELY**

GOVERNMENT RESPONSE TO VICTORIAN LAW REFORM COMMITTEE'S THREE "CURBING THE PHOENIX COMPANY" REPORTS DATED JUNE 1994 AND MAY AND NOVEMBER 1995 RESPECTIVELY

BACKGROUND

The Reports

1. The Victorian Law Reform Committee (Committee) was given the terms of reference for these reports on 16 March 1993. These terms of reference are detailed at the Annexure to this Response.
2. The Committee delivered its First Report in June 1994. The interim response of the Government to that report was tabled in Parliament on 28 February 1995. At that stage the Government determined that it would not consider in detail or respond to the recommendations made by the Committee pending the publication of the Second Report.
3. The Committee's Second Report, delivered in May 1995, examines the practice of overseas jurisdictions such as Canada, the United Kingdom and New Zealand. The Committee has endorsed in essence the recommendations made in the First Report, but as a result of its investigation into measures adopted by the jurisdictions mentioned, they have expanded many of the recommendations made in the First Report.
4. The Committee's Third Report, delivered in November 1995, reviews the proposals of the Commonwealth Attorney-General's Corporations Law Simplification Task Force (Task Force) to deal with the "phoenix company" phenomenon and its regard to the Committee's recommendations, particularly in relation to company officers and related party transactions.
5. The Government wishes to take this opportunity to respond to all three Reports, bearing in mind that the Second Report endorsed the First Report recommendations, subject to a few additions and substitutions.

INTRODUCTORY COMMENTS

6. The Reports identified the practice of "phoenix companies" (that is companies which fail, are unable to pay their debts or fulfill their obligations to employees, but which then reappear, in another guise, with substantially the same management and sometimes with the same staff) and the consequences of this phenomenon.
7. The efforts of the Committee are appreciated by the Government which agrees that the phoenix company phenomenon is undesirable as it constitutes a disincentive to business development, a burden on small business and undermines public confidence in Government

regulation of companies. The Government believes that one of the major benefits of the Committee's Reports will be to raise the level of public awareness of the incidence of the phoenix company and to bring the matter into the public arena for consideration and debate. To this end the Government notes that, largely as a result of the Victorian inquiry, measures to deal with the phenomenon are planned at the Commonwealth level with the involvement of the Ministerial Council for Corporations (MINCO) and the Commonwealth Attorney-General's Corporations Law Simplification Task Force (Task Force). The Government further notes that the exact nature of the MINCO response is yet to be formulated but that it appears the Committee's recommendations are being dealt with in a serious and constructive fashion.

8. In any examination of the law relating to corporations in Australia, it is necessary to understand and appreciate the legislative regime in which corporations operate. The regulation of corporate activity is part of a **national scheme** designed to provide a uniform environment in which corporations conduct their business. All the States and Territories have legislation in place which adopts the Commonwealth *Corporations Law*. In Victoria the legislation is the *Corporations (Victoria) Act 1990*. Under the national scheme, all amendments to the Commonwealth legislation must be approved by MINCO, on which the Commonwealth Government has the deciding vote. Thus, when examining the recommendations made by the Committee, it is clear that there are limitations imposed by Victoria's participation in the national scheme. In one important sense these limitations are also a great benefit in that the phoenix phenomenon **must** be dealt with on a uniform, national basis and not differently by different jurisdictions.
9. The Recommendations of the Committee can be divided, for simplicity, into two categories:
 - (i) the recommendations requiring the approval and action by MINCO (which may require additional State action after this approval); and
 - (ii) the recommendations which specify measures that may be acted upon by the Government at the State level;
10. Part I of this Response discusses the recommendations falling into category (i), and notes the primary role of MINCO in any corporate reform. Part II discusses the recommendations falling into category (ii), which require specific Victorian initiatives, and assesses the practical and economic viability of each of these recommendations. Part III of this Response discusses the Committee's comments on the Task Force proposals in its Third Report. Please refer to Table A in the Annexure, at the beginning of the text of the Committee's recommendations reproduced from the first two Reports. Table A lists all the recommendations and directs the reader to the Parts and paragraphs in this Response where that recommendation is addressed.

PART I: Committee Recommendations Requiring MINCO Approval and Initiative

11. The recommendations considered in this Part involve changes to the *Corporations Law*. Please see the Annexure for the full text of these recommendations. The recommendations of the Committee have been appropriately referred for consideration by the Minister for Fair Trading to the Commonwealth Attorney-General, the ASC, the Simplification Task Force and other members of MINCO. The fact that the Committee has been and will continue to be directly consulted in stage 3 of the simplification process indicates the high regard held for the work they have undertaken, and the value of their recommendations. Victoria cannot initiate changes to its own Corporations legislation without jeopardising the national corporate scheme. Even if Victoria could "go it alone", the efficacy of such action would be limited given the national nature of the Corporations Law. Any changes proposed to be made to the national companies and securities law scheme require the approval of the Commonwealth.
12. The Minister for Fair Trading referred to the reports of the Committee at the Thirteenth Ordinary Meeting of MINCO in July 1995. Further, she requested the issue of phoenix companies be expressly included as a future agenda item of the meeting. At that meeting, the Commonwealth Attorney-General (Mr Michael Lavarch) advised that the Simplification Task Force would consider the provisions relating to disqualification of company directors in Stage 3 of its program. The meeting noted that Mr Lavarch would ask the Simplification Task Force to consult directly with the Committee in relation to their recommendations on Phoenix companies which are relevant to Stage 3 of the program.
13. The Convenor of the Simplification Task Force and other officers of the Attorney-General's Department met with representatives of the Committee, including the Chairman (the Hon James Guest MLC) on 4 September 1995. At that meeting the recommendations of the Committee were discussed in light of the Task Force's work to date on recommendations for the reform of the law on disqualification of company directors. The Committee was advised of the intention to discuss a reform proposal with the Simplification Consultative Group on 20 September, with a view to its release in October. It was noted that the Committee had an ongoing interest in this topic and that further comments would be welcomed. The Task Force released its proposals with respect to these issues in October 1995, which are referred to in Part III of this Response.
14. The Government agrees with the suggestion that the Third Simplification Bill will be the appropriate legislative vehicle for changes to the law that may be proposed in this regard. The Simplification Task Force will undertake direct consultation with the Committee, and welcomes comments on its proposals. Further, the Commonwealth will consult and obtain the approval of MINCO for the Bill which will be introduced to amend the Corporations Law.
15. In addition to these developments, the ASC announced on 29 June 1995 that it will be targeting Phoenix companies in its Community Response Project. This is a series of new

programs, designed to target and direct resources towards particular sections of the market and business community that are identified as requiring attention to ensure that the ASC meets the needs of the community as a whole. It is particularly designed to help improve compliance with the Corporations Law at the 'smaller end of town'. The priorities identified and the programs implemented to address them will be reassessed on a six monthly basis.

PART II: Committee Recommendations Requiring Victorian Initiatives

16. Report 1, recommendation 4:
That the Victorian Government should seek a review of the resources devoted to detecting and prosecuting persons who involve themselves in the management of companies while disqualified
AND
Report 1, recommendation 5
That the Victorian Government should take steps to change the public and judicial attitudes to culpable mismanagement of corporations and abuse of the corporate form, so that persons who manage companies when disqualified or whose culpable management leads to serious losses to creditors are as likely to go to prison as those who deprive others of their money by theft.
17. Both of the above recommendations derive from the Committee's view that so called "white collar crime" is not currently treated as truly criminal behaviour. This in turn leads to the view that severe penalties are not imposed when people are brought before the Courts. A greater appreciation of the true cost of corporate crime would be of benefit to the community, if it resulted in higher sentences, as it may deter would-be offenders. However, in the present economic climate it may be difficult to justify expenditure of scarce resources where the benefit is hard to quantify and in isolation may be ineffective.
18. Recommendation 4 of the First Report only speaks in terms of a review, but there is little point in a review if further action may not be forthcoming. This Government does take corporate crime seriously and has expended considerable effort in its investigation and prosecution, for example, by the enhancement of the activities of the specific purpose multi-disciplinary corporate crime group within the Victoria Police.
19. Recommendation 5 in the first report suggests that the Government take steps to change public and judicial attitudes to culpable mismanagement of companies. Although this may be a worthy cause, such a change is difficult to achieve and would, in isolation from other changes, achieve very little. Such a change is most likely to flow from public and judicial observance of changed legislation and it is this that should be the first step to be followed.
20. Report 1, recommendation 6:
That the Victorian Government should encourage the ASC to give a higher priority to developing computer programs to detect disqualified persons becoming involved in the

management of companies, and should seek the support of MINCO to require all directors of limited liability companies to have and use a unique identity number.

21. The Government supports the view that changes in legislation need to be supported by practical steps to ensure that the objectives of the legislation are implemented. However, operational priorities of the ASC are a matter for the Commonwealth Government to determine. Since the Commonwealth has now recognised the extent of the phoenix company problem, the ASC should consider giving a higher priority to a computer program along the lines recommended by the Committee. The Minister for Fair Trading will raise this matter at MINCO for consideration.
22. An issue which clearly needs more deliberation and discussion within the wider community is that part of the recommendation which concerns identification numbers. This concept has overtones of an identity card and at this stage the Government would not support the idea without evidence of wide business and community support. The questions of a unique identity number and better identification of directors are under active consideration by the Simplification Task Force.
23. Report 1, recommendation 12:
That the Victorian Government fund Small Business Victoria to investigate the dimensions of the risk to small business posed by the phoenix company phenomenon, and to develop and evaluate a training package to help small business to improve their credit assessment and credit management.
AND
Report 2, recommendation 8:
The Committee recommends that the Victorian Government should fund Small Business Victoria and the Office of Fair Trading and Business Affairs to design and conduct education and advertising programs targeted at those most at risk, and aimed at increasing general public awareness of the risks that may be inherent in dealing with limited liability companies.
24. This proposed initiative is in two parts. The first would require the Government to commit funding to a project which may be very costly without significant or quantitative benefit. The Government's view is that greater returns for business would flow from more effective prosecutions and changes to the corporate culture across the national spectrum rather than localised projects. Such a change, as referred to above, is best fostered after legislative changes occur. The second part of the recommendation would need to be part of a package of training for intending small businesses. This type of training is needed in all aspects of management of companies and any funding provided to Small Business Victoria should be targeted to lifting all round credit management, not just in dealing with the phoenix company problem.
25. The Government will continue to liaise with Small Business Victoria and, where appropriate, the Office of Fair Trading and Business Affairs, to investigate the viability of this part of the recommendation. However the Government wishes to emphasise its view

that **national** education and advertising programs as part of the contemplated national corporate simplification and reform program, would be more appropriate for addressing the phoenix company phenomenon.

26. Report 1, recommendation 13:
That the Victorian Government investigate requiring State licensing and registration bodies to take account of a persons previous involvement with a company which has failed without paying its creditors.
27. The Government notes that all Licensing bodies administered out of the Office of Fair Trading and Business Affairs already take into account a person's previous involvement in a company that was unable to pay its debts. The Government will endeavour to ensure that this criterion will also be taken into account for the issue of all other business related licences. This recommendation should also be read in light of the recommendations to be considered by MINCO. Further action by Government may be contemplated after the Commonwealth position has been confirmed with regard to office holders and related party transactions, and, later to directors themselves.
28. Report 1, recommendation 8:
That when a liquidator takes a bona fide action against directors or managers of a corporation to recover property of the corporation or to secure compensation for the corporation the Court should not be able to make an order for costs or an undertaking as to damages against the liquidator personally, and the inability of the corporation to provide security for costs or damages should not be a bar to the action proceeding; but that such an action should be subject to the leave of the Court; and that in these circumstances the costs and damages of a successful defendant should normally have priority over all other claims on the corporation's assets.
29. The Government is of the opinion that the implementation of this recommendation could further strengthen the action against management by liquidators. However, the part of this recommendation that recommends that the Court should not be able to make an order for cost against the liquidator personally must be considered in light of the Government's general policy of not providing "financial immunity" to persons who provide services for remuneration, except in exceptional circumstances. To determine whether exceptional circumstances exist in the context of the phoenix company phenomenon, the following factors should be investigated:
 - the ability of aggrieved parties to seek redress;
 - the availability of insurance (in this case, private indemnity insurance);
 - the public benefit of the service provided; and
 - the current willingness of persons to perform the service.

30. The Government will also seek the views of the judiciary as to whether:
- (a) the recommendation could have the potential to lead to injustice to directors who are ultimately found to be blameless where a liquidator, as trustee for the creditors of the failed company, has no company funds to pay their costs; and
 - (b) the notion of the liquidator undertaking a “bona fide action” would be too difficult to decide in any court challenge.
31. Report 1, recommendation 10:
That the enforcement of money judgments be made the subject of a separate inquiry.
32. The Government agrees that this is a much wider topic than the one with which the Committee was mainly concerned. However, the recommendation is not supported because the topic closely interacts with insolvency and was the subject of an exhaustive report by the Australian Law Reform Commission (No. 45). A further inquiry along such similar lines does not appear to be warranted so soon afterwards.
33. Report 1, recommendation 11:
That Victoria legislate to place restrictions on the use of business names similar to those of a failed corporation by persons associated with the failed corporation, except by leave of the court, based on section 216 and 217 of the Insolvency Act 1986 (United Kingdom); and that the Victorian Government seek to persuade the other Australian jurisdictions to do likewise.
34. The Government believes this recommendation could have been considered at Commonwealth level in the drafting of the Second Corporate Law Simplification Bill - with respect to company names. However, since the Commonwealth is firmly committed to the application of the identical names test for company names, it may not obtain MINCO approval. The matter will, however, be raised at MINCO by Victoria. If Victoria were to adopt this recommendation in respect of the registration of business names, the effectiveness would be off-set by the fact that there would be no similar policy applying to the registration of company names in the *Corporations Law*.
35. Report 1, recommendation 14
That:
- *the Government allocate funds to establish a 12 month pilot program within the State Revenue Office or the WorkCover administration to provide funds to liquidators to do more detailed investigations and report on failed companies where there may be an action against the directors or managers, and where appropriate to take action to recover assets from them;*
 - *the goal of the pilot be to assess whether successful recovery actions would recover sufficient money (where the debts would previously have been written off) to cover the costs of the unsuccessful investigations and actions; and*

- *the Government report to the Parliament within twelve months of the conclusion of the pilot program whether the pilot program meets its objectives, giving details of the costs, the number of phoenix companies detected, the amounts received for the State and the amounts received for business creditors who would otherwise have got nothing.*
36. The Government is aware that the State loses tens of millions of dollars annually in unpaid payroll tax and WorkCare or WorkCover premiums owing by failed companies. The recommendation contemplates two actions by Government: first, the funding of an exploratory pilot program within the State Revenue Office or WorkCover to establish the scope for cost-effective investigations; and second, to report to Parliament on the results, including the numbers of phoenix companies.
 37. While the proposal has merit, the Government does not support the recommendation on the grounds of efficacy. Both the State Revenue Office and the WorkCover administration already have in place debt recovery procedures in line with prudent commercial practice. These Offices will be asked by Government to provide information as to the number and type of "phoenix companies" with which they deal.
 38. Report 2, recommendation 9
The Committee recommends that the Victorian Government should take steps to increase the general public awareness of the use that can be made by persons dealing with limited liability companies, of guarantees which are designed to protect those persons' financial position. The preparation and distribution of a standard form of guarantee to be given by company directors to secure their company's financial liabilities, would be a cost-effective means of improving the situation of creditors, especially those likely to be confronted by the phoenix company phenomenon.
 39. The Government believes that this proposal has merit, but should be undertaken more effectively at the national level, as part of the publicity for the intended corporate reform. The Minister for Fair Trading will raise this matter at MINCO for consideration.

PART III: THE THIRD "CURBING THE PHOENIX COMPANY" REPORT DATED NOVEMBER 1995

40. The Task Force published its proposal for simplifying the provisions of the Corporations Law relating to company officers and related party transactions in October 1995. In presenting its proposals the Task Force acknowledges that it has taken account of the Committee's recommendations. In its Third Report, the Committee examined and commented on these proposals of the Task Force.
41. The terms of the Proposal are set out in Annexure A. Briefly, the Proposal proposed new provisions in place of sections 229, 599 and 600 of the Corporations Law along the following lines:

- (i) Creating an ASC power to disqualify directors and managers of companies for up to 10 years where fault has occurred that caused the failure of the company to pay its debts.
 - (ii) Automatic disqualification from managing a company for ten years if a person has been convicted of any of a number of specified offences.
 - (iii) Disqualification from managing a company where any of a number of specified acts relating to the bankruptcy law are committed.
42. The Government notes that the Committee has been able, through its Reports, to advance important reforms to the Corporations Law. The Government notes the primary role of MINCO, which has issued a discussion paper in November 1995 relating to officers of companies, some proposals of which specifically relate to the phoenix company problem. The Commonwealth Government has recognised the value of the Committee's extensive recommendations.
43. Due to the calling of the Federal election in March, work in relation to phoenix companies, such as preparation of discussion proposals and a draft Bill, was postponed and can probably be expected for comment in the middle of this year. Therefore the Government reserves its final comments until policy is more developed. The Government hopes to continue to work with MINCO on the issue of the phoenix company phenomenon in the future.

CONCLUSION

44. The impetus for the terms of reference given to the Committee was the recognition by both the Premier and the Minister for Fair Trading that the phoenix company phenomenon is not only a cost to business but has wider implications for the economy. The Government recognised that the phenomenon distorted the level playing field it was trying to create in Victoria by allowing some businesses to walk away from their debts and forcing creditors to carry debts which could not be recovered. The Reports of the Committee have supported and reinforced the Government's initial view.
45. As outlined, the issues which arise through the phoenix company are now firmly on the national corporations law agenda. The three Reports of the Committee are in no small way responsible for this new awareness. The Committee's views are being sought by the Commonwealth as it embarks on the third stage of its simplification process. The Government will seek to encourage and maintain the impetus that the Reports have begun.
46. In relation to those initiatives that the Victorian Government could undertake, the Government, as stated, will continue to explore the options which it believes have practical merit and will implement those options which it then considers would benefit the

Victorian economy. As noted, however, any action taken by the Government must not infringe on the Government's commitments to the national corporations law scheme.

47. The Government takes this opportunity to thank the Committee for their efforts in undertaking this complex and difficult reference.

ANNEXURE

THE VICTORIAN LAW REFORM COMMITTEE "CURBING THE PHOENIX COMPANY" REPORTS

TERMS OF REFERENCE

Terms of reference for this report were given to the Law Reform Committee on 16 March 1993. The Committee were requested to inquire into and report to Parliament as to -

- 1.1 The adequacy of the existing disqualification procedures where company directors and persons acting in the management of companies have been involved in failed companies and in particular the adequacy of section 599 of the Corporations Law as a means of achieving creditor protection.
- 1.2 The adequacy of penalties imposed where disqualified persons act in the management of companies.
- 1.3 The adequacy of existing supervisory and enforcement arrangements in relation to disqualified persons.
- 2.1 Whether the Corporations Law provides appropriate remedies against directors and effective execution against directors' personal assets where those directors have been involved in the management of companies which have failed to meet financial obligations.
- 2.2 Whether the Corporations Law provides appropriate means of tracing, for the benefit of creditors, assets divested by company directors.
- 2.3 Whether the Supreme Court of Victoria and the Federal Court of Australia are appropriate forums for civil actions against directors (for instance under section 592 of the Corporations Law) having regard to the costs of such actions.
- 2.4 What other safeguards might be introduced to protect creditors in their dealings with companies.
- 3.1 The means by which Victoria might implement any recommendations arising out of this inquiry.

RECOMMENDATIONS OF THE VICTORIAN LAW REFORM COMMITTEE

Table A: Index to Government Response to Recommendations in Reports 1 & 2

REPORT 1	GOVERNMENT RESPONSE
Recommendation 1	Part I ¹
Recommendation 2 (substituted by Recommendation 4 in Report 2)	Part I
Recommendation 3 (substituted by Recommendation 3 in Report 2)	Part I
Recommendation 4	Part II ² , paragraphs 16-19
Recommendation 5	Part II, paragraphs 16-19
Recommendation 6	Part II, paragraphs 20-22
Recommendation 7	Part I
Recommendation 8	Part II, paragraphs 28-30
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Recommendation 10	Part II, paragraphs 31-32
Recommendation 11	Part II, paragraphs 33-34
Recommendation 12	Part II, paragraphs 23-25
Recommendation 13	Part II, paragraphs 26-27
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REPORT 2	
Recommendation 1 (makes substitutions only)	
Recommendation 2	Part I
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Recommendation 6	Part I
Recommendation 7	Part I
Recommendation 8	Part II, paragraphs 23-25
Recommendation 9	Part II, paragraphs 38-39

¹ Proposals requiring MINCO approval and Commonwealth Government initiative

² Proposals requiring Victorian initiative

FIRST REPORT

Recommendation 1

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the Corporations law so that the directors of a failed company which is struck off without a formal liquidation and which pays less than 50c in the dollar of its liabilities are subject to the same sanctions as if there had been a formal liquidation and an adverse liquidator's report.

Recommendation 2

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the disqualification provisions in s. 600 of the Corporations Law. There should be two levels: where a corporation is liquidated and pays less than 50c in the dollar of its liabilities the ASC should have a discretion to require a director of the corporation to show cause why he or she should not be disqualified; and when a person is involved as a director or manager in two such insolvencies the disqualification should be automatic unless the director can satisfy the ASC otherwise.

Recommendation 3

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to section 599 of the Corporations Law. That section should enable the Court to disqualify if satisfied at the civil standard of the matters of mismanagement now requiring proof beyond reasonable doubt, and in the event of only a single insolvency.

Recommendation 4

The Committee recommends that the Victorian Government should seek a review of the resources devoted to detecting and prosecuting persons who involve themselves in the management of companies while disqualified.

Recommendation 5

The Committee recommends that the Victorian Government should take steps to change the public and judicial attitudes to culpable mismanagement of corporations and abuse of the corporate form, so that persons who manage companies when disqualified or whose culpable management leads to serious losses to creditors are as likely to go to prison as those who deprive others of their money by theft.

Recommendation 6

The Committee recommends that the Victorian Government should encourage the ASC to give a higher priority to developing computer programs to detect disqualified persons becoming involved in the management of companies, and should seek the support of the Ministerial Council to require all directors of limited liability companies to have and use a unique identity number.

Recommendation 7

The Committee recommends that the Victorian Government should take steps by itself and in cooperation with the other members of the Ministerial Council to secure wider and more regular dissemination of the register of disqualified directors, and should urge banks and other financial institutions to make use of this information so as to make it harder for disqualified persons to manage companies.

Recommendation 8

The Committee recommends that when a liquidator takes a bona fide action against directors or managers of a corporation to recover property of the corporation or to secure compensation for the corporation the Court should not be able to make an order for costs or an undertaking as to damages against the liquidator personally, and the inability of the corporation to provide security for costs or damages should not be a bar to the action proceeding; but that such an action should be subject to the leave of the Court; and that in these circumstances the costs and damages of a successful defendant should normally have priority over all other claims on the corporation's assets.

Recommendation 9

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the Corporations Law to create a statutory process analogous to a Mareva injunction to enable the courts to freeze assets of a director or manager which are prima facie assets on which the corporation has a just claim.

Recommendation 10

The Committee recommends that the enforcement of money judgments be made the subject of a separate inquiry.

Recommendation 11

The Committee recommends that Victoria legislate to place restrictions on the use of business names similar to those of a failed corporation by persons associated with the failed corporation, except by leave of the court, based on section 216 and 217 of the Insolvency Act 1986 (United Kingdom); and that the Victorian Government seek to persuade the other Australian jurisdictions to do likewise.

Recommendation 12

The Committee recommends that the Victorian Government fund Small Business Victoria to investigate the dimensions of the risk to small business posed by the phoenix company phenomenon, and to develop and evaluate a training package to help small businesses improve their credit assessment and credit management.

Recommendation 13

The Committee recommends that the Victorian Government investigate requiring State licensing and registration bodies to take account of a person's previous involvement with a company which failed without paying its creditors.

Recommendation 14

The Committee recommends

- *that the Government allocate funds to establish a 12 month pilot program within the State Revenue Office or the WorkCover administration to provide funds to liquidators to do more detailed investigations and report on failed companies where there may be an action against the directors or managers, and where appropriate to take action to recover assets from them.*
- *that the goal of the pilot be to assess whether successful recovery actions would recover sufficient money (where the debts would previously have been written off) to cover the costs of the unsuccessful investigations and actions.*
- *that the Government report to the Parliament within twelve months of the conclusion of the pilot program whether the pilot program meets its objectives, giving details of the costs, the number of phoenix companies*

detected, the amounts received for the State and the amounts received for business creditors who would otherwise have got nothing.

SECOND REPORT

Recommendation 1 (Confirmation of Previous Recommendations)

The Committee recommends that Recommendation 3 and Recommendation 4 of this report be substituted respectively for Recommendation 3 and Recommendation 2 of the First Report. Otherwise the Recommendations made in the First Report be confirmed.

Recommendation 2 (Corporations Considered to be at Risk of Financial Failure)

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the Corporations Law by the inclusion of provisions similar to those contained in the New Zealand Corporations (Investigation and Management) Act 1989 which apply to corporations considered to be at risk of financial failure and which seeks to prevent further deterioration in the financial affairs of those corporations and to protect the public interest.

Recommendation 3 (Disqualification of Directors by the Court)

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the Corporations Law by the inclusion of a provision which deals with the duty of a court to disqualify a person from acting as a company director where that person has been a director of an insolvent corporation and his or her conduct as a director makes him or her unfit to continue acting in the management of any corporation. Such a provision should be in substitution for section 599 of the Corporations law and should be modeled on section 383 of the New Zealand Companies Act 1993.

Recommendation 4 (Disqualification of Directors by the Commission)

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the Corporations Law by replacing section 600 of the Corporations Law with a provision similar to that contained in section 385 of the New Zealand Companies Act 1993 which deals with the exclusion by the regulatory authority of certain persons from the management of companies. However, the Committee recommends that, in lieu of the New Zealand provision's requirement that a person may be prohibited by the regulatory authority from being a director or promoter of a company if he/she has taken part in the management of two or more failed companies, there should be a two tiered approach: where a corporation is liquidated and pays less than fifty cents in the dollar or its liabilities the ASC should have a discretion to require a director to show cause why he or she should not be disqualified; and when a person is involved as a director or manager in two such insolvencies the disqualification should be automatic unless the person can satisfy the ASC otherwise.

Recommendation 5 (Disqualification of Directors on Conviction)

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for an amendment to section 299 of the Corporations Law, which currently provides that on conviction for certain specified offences a person is disqualified from managing a corporation for a period of five years. The Committee recommends that there should be a minimum disqualification period of two years and an increased maximum disqualification period of fifteen years.

Recommendation 6 (Assetless Companies Fund)

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for the establishment of an Assetless Companies Fund as recommended by the Australian Law Reform Commission in its Report No. 45, General Insolvency Inquiry (1988) to provide a fund from which payments could be made so as to enable the winding up of and investigations into insolvent assetless companies.

Recommendation 7 (Grouping of Provisions relating to Directors)

The Committee recommends that the Victorian Government should seek the support of the Ministerial Council for a change to the Corporations Law which would ensure that all provisions dealing with directors duties, obligations, liabilities, disqualification and associated offences and penalties are contained within the one part of the Corporations Law.

Recommendation 8 (Public Awareness Education and Advertising Programs)

The Committee recommends that the Victorian Government should fund Small Business Victoria and the Office of Fair Trading Business Affairs to design and conduct education and advertising programs targeted at those most at risk, and aimed at increasing general public awareness of the risks that may be inherent when dealing with limited liability companies.

Recommendation 9 (Increasing Public Awareness of the Use of Guarantees)

The Committee recommends that the Victorian Government should take steps to increase the general public awareness of the use that can be made by persons dealing with limited liability companies, of guarantees which are designed to protect those persons' financial position. The preparation and distribution of a standard form of guarantee to be given by company directors to secure their company's financial liabilities, would be a cost effective means of improving the situation of creditors, especially those likely to be confronted by the phoenix company phenomenon.

CORPORATIONS LAW SIMPLIFICATION TASK FORCE PROPOSALS

(Extracted from the Committee's Third "Curbing the Phoenix Company" Report, November 1995)

1. The Task Force published its proposal for simplifying the provisions of the Corporations Law relating to company officers and related party transactions in October 1995.
2. Under the proposal sections 229, 599 and 600 of the *Corporations Law* will be replaced by the following provisions -
 - (i) A power in the Australian Securities Commission (ASC) to disqualify a person from being a director or managing a company for up to ten years if the ASC is satisfied, inter alia, that the person was a director or executive officer of a corporation which was deregistered by the ASC for failing to lodge documents with creditors not being fully paid, or which was wound up with creditors not being fully paid, or which ceased to carry on business because of its inability to pay its debts, and in any of these situations the corporation was mismanaged and the director's or executive officer's conduct in relation to the management, business or property of one or more corporations justifies the disqualification.
 - (ii) A person will be automatic [sic] disqualified from managing a company for ten years if a person has been convicted of any of a number of specified offences. The ASC will have a discretion to reduce the period from ten to a minimum of two years.

- (iii) A person will be disqualified from managing a company if he or she commits any of a number of specified acts relating to the bankruptcy law.
3. If adopted these proposals will give effect to a number of the recommendations made in the Committee's Reports as follows -
- (i) The extension of the disqualification provision to directors of companies which are deregistered by the ASC without a formal liquidation.
- (ii) The extension of the disqualification provisions to cover directors involved in one company failure. Under the existing provisions the director must have been involved in the management of two companies that fail. The Task Force agreed with the Committee's recommendation to this effect on the basis of the discretionary nature of the ASC's power to disqualify.
- (iii) The increase in the disqualification period because of a conviction of an offence from five to ten years. The Committee recommended an increased maximum disqualification period of fifteen years and a minimum disqualification period of two years. The Task Force has settled on a maximum of ten years, but has raised specific issues as to whether disqualification periods should be adopted instead of the ten years preferred by the Task Force.
- (iv) It is likely that the Task Force's proposals will bring together in the one part of the Corporations Law all the provisions relating to the disqualification of company directors. This is in accord with Recommendation 7 of the Committee's Second Report.
4. Another aspect of the Task Force's review of the directors' disqualification provisions in the Corporations Law is still to be resolved, that is, the re-use of the names of failed companies by people associated with those companies. A recommendation regarding this issue was made in the Committee's First Report as follows -

That Victoria legislate to place restrictions on the use of business names similar to those of a failed corporation by persons associated with the failed corporation, except with leave of the court, based on sections 216 and 217 of the Insolvency Act 1986 (United Kingdom); and that the Victorian Government seek to persuade the other Australian jurisdictions to do likewise.