Insolvency Law Update

The chimera of restructuring reform: An opportunity missed for MSMEs in pt 5.3B

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I Introduction

In 1993, corporate rescue was modernised with the introduction of pt 5.3A of the *Corporations Act 2001* (Cth) ('*Corporations Act*'). It is true to say that the new debt restructuring procedure was 'embraced' by those who could access it — companies and their directors, those who would administer it — registered liquidators and those whose debts would be attended to and perhaps paid in part — creditors. In the first 4 months of pt 5.3A, there were 142 appointments.[1] On 1 January 2021, pt 5.3B commenced which introduced a new small business restructuring process that includes the appointment of a small business restructuring practitioner to companies with liabilities of less than $1 million and acceptance of a restructuring plan by creditors. There have been five appointments in the first 4 months of the new pt 5.3B small business restructuring.[2] There is concern even at this early stage that this new regime is not going to work efficiently or effectively and is not going to be embraced by companies and their directors, registered liquidators and creditors, unlike what we experienced in 1993.[3]

Even before this year's new Part, there were, and continue to be, widespread concerns with corporate rescue and insolvency laws in Australia.[4] Some of the concerns raised relate to the low returns to creditors (more likely than not, no returns),[5] a concern that the cost of the insolvency rescue

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1 See Jason Harris, 'Comparing the Start of Parts 5.3A and 5.3B', *Australian Insolvency Law* (Blog Post, 20 April 2021) <https://australianinsolvencylaw.com/2021/04/20/comparing-the-start-of-parts-5-3a-and-5-3b/>.

2 Ibid.

3 The Treasury was advised that the new procedure had issues that would hinder its effectiveness — see the submissions on the proposal law: 'Insolvency Reforms to Support Small Business', *Treasury (Cth)* (Web Page, 7 October 2020) <https://treasury.gov.au/consultation/c2020-118203>.

4 See, eg, 'Insolvency Practices Inquiry', *Australian Small Business and Family Enterprise Ombudsman* (Web Page, July 2020) <https://www.asbfeo.gov.au/inquiries/insolvency-practices> ('Insolvency Practices Inquiry'); John Winter, 'Simple, Efficient, Effective: A Call for Reform' (2018) 30(4) *Australian Restructuring Insolvency and Turnaround Association Journal* 16; Jason Harris, 'Should Voluntary Administration Remain a One-Size-Fits-All Procedure? Do We Need a Fast Track System for Small Business Rescues?' in Shelley Griffiths, Sheelagh McCracken and Ann Wardrop (eds), *Exploring Tensions in Finance Law: Trans-Tasman Insights* (Thomson Reuters, 2014) 101–26 ('Should Voluntary Administration Remain a One-Size-Fits-All Procedure?').

5 Jason Harris, 'Corporate Insolvency by the Numbers', *Australian Insolvency Law* (Blog

procedure makes it unviable, a lack of trust in the insolvency practitioners (certainly true in some quarters like politicians and the media), creditors who are rationally apathetic and disengaged, procedures that are complex, time-consuming and bureaucratic, and a lack of input and control from those already running the company.[6]

Since 1993 corporate rescue has been a one-size-fits-all and this leads to criticism that it doesn't meet the needs or expectations of small business.[7] Corporate MSMEs (micro-, small- and medium-sized enterprises) have different features that make corporate rescue different to larger companies[8] such as their low asset base (and often value comes from owner/manager's goodwill), that they are 'too poor to go broke!' in that they have poor revenue in addition to their low asset base, and they may not have secured creditors or at least ones that are willing to assist resulting in limited financing and refinancing options. MSMEs often will have family and therefore sentimental attachment to the company and would not want the company to fail or for them to lose control during a restructuring, they will have personal guarantees provided by their directors and many mix business and personal assets.[9] Additionally, there are MSMEs who rely on poor information systems, have poor management skills, unpaid tax debts, a lack of customer diversification and operate on wafer-thin margins.[10] MSMEs may also operate in low-margin and competitive industries where they may not have a market leading position which may make them unattractive to private equity and distressed debt funders. It is in this environment and a lingering COVID-19 pandemic that the new pt 5.3B has been introduced.[11]

II The new pt 5.3B from 1 January 2021

The Explanatory Memorandum for pt 5.3B expresses that

> [t]he intention of the debt restructuring process is to provide an alternative to the 'one-size-fits-all' voluntary administration regime for small [non-complex] businesses. It reduces the complexity and cost of the administration process, providing a greater role for the company directors during the process and allowing them to retain control over the company throughout. These changes are intended to

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Post, 27 February 2018) <https://australianinsolvencylaw.com/2018/02/27/corporate-insolvency-by-the-numbers/>.

6 See 'Insolvency Practices Inquiry' (n 4).

7 Harris, 'Should Voluntary Administration Remain a One-Size-Fits-All Procedure?' (n 4).

8 See further World Bank Group Insolvency and Creditor/Debtor Regimes Task Force, *Report on the Treatment of MSME Insolvency* (Report, 2017); Riz Mokal et al, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (Oxford University Press, 2018).

9 Australian Small Business and Family Enterprise Ombudsman, *Inquiry into Small Business Loans* (Inquiry Report, 12 December 2016).

10 Stephen Parbery, 'Assessing Voluntary Administration in Australia: Including Suitability for Workouts, Turnarounds and Pre-packs' in RP Austin and Fady JG Aoun (eds), *Restructuring Companies Troubled Times: Direct and Creditor Perspectives* (Ross Parsons Centre of Commercial, Corporate and Taxation Law, 2013) 99–101.

11 Josh Frydenberg and Michael Sukkar, 'Insolvency Reforms to Support Small Businesses Recovery' (Joint Media Release, 24 September 2020) <https://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/media-releases/insolvency>.

> encourage more small businesses to seek debt restructuring earlier, increasing their chances of recovering viability.[12]

Whilst this suggests the new Part provides an alternative to voluntary administration, it does draw heavily on pt 5.3A and existing case law will be persuasive and helpful.

The Treasurer has promised that this will be 'a single, simpler, faster, more cost-effective insolvency process for small business' and 'a move to a more flexible "Debtor in Possession" model'[13] enabling 'small business owners to remain in control' whilst providing them with an opportunity to restructure.[14]

There are some very positive provisions within the new pt 5.3B. For example, s 452A boldly states the object of the Part is to

> provide for a restructuring process for eligible companies that allows the companies:
> (a) to retain control of the business, property and affairs while developing a plan to restructure with the assistance of a small business restructuring practitioner; and
> (b) to enter into a restructuring plan with creditors.

Given the use that is made of s 435A in pt 5.3A which has similar wording, this provision too could be expected to be used in conjunction with other provisions to assist in litigation. Furthermore, the stated purpose of small business restructuring stands in contrast to the goals of voluntary administration because the new procedure is aimed at simply providing an opportunity for a plan to be put to creditors, not with trying to save the MSME (as the goals of pt 5.3A state as their top priority).

Another example of what may turn out to be one of the mostly used provisions is s 458A. This is essentially the same as pt 5.3A s 447A, which provides the court with a general power to make orders.[15] The same wording as is used in s 447A, namely '[t]he Court may make such order as it thinks appropriate about how this Part is to operate in relation to a particular company' and any order can be made subject to conditions. This allows the court to effectively alter how the legislation works in relation to a particular company.[16] This section can be used by application from the company, creditors, the restructuring practitioner, the Australian Securities and Investments Commission or any other interested party. Based on the experience with the widespread use of s 447A since the introduction of voluntary administration, this new s 458A will be a frequently used tool to assist both MSMEs and their restructuring practitioners in trying to address the MSMEs' financial difficulties.

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12 Explanatory Memorandum, Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (Cth) 13 [1.3].

13 For a discussion of the debtor-in-possession model in the United States, see Jason Harris, 'Restructuring Nirvana? Chapter 11 Bankruptcy and Australian Insolvency Reform' (2015) 16(3) *Insolvency Law Bulletin* 42; Ahmed Terzic, 'Turning to Chapter 11 to Foster Corporate Rescue in Australia' (2016) 24(1) *Insolvency Law Journal* 5.

14 See Frydenberg and Sukkar (n 11).

15 See further Jason Harris, 'The Constitutional Basis of s 447A: Is It a Power without Limit?' (2006) 14(3) *Insolvency Law Journal* 135.

16 *Australasian Memory Pty Ltd v Brien* (2000) 200 CLR 270.

III How will the new procedure work?

The new procedure in pt 5.3B involves three phases:

(1) the *restructuring phase*, which is when the restructuring plan is being formulated by the debtor company[17] — The company has 20 business days to put its restructuring proposal to the creditors from the date of the restructuring practitioner's appointment (referred to in the legislation as 'the proposal period').[18] The restructuring practitioner or the court may extend this 20-business day proposal period.[19]

(2) the *acceptance phase*, which is when creditors are asked to vote for or against the restructuring plan proposed by the company[20] — This occurs during the company's restructuring period and will end if the creditors reject the restructuring plan, if a plan is not put to the creditors within the 20-business day proposal period or if the restructuring practitioner cancels the restructuring.[21]

(3) the *plan implementation phase*, which is when the company is operating under a restructuring plan[22] — The plan implementation phase begins at the end of the last day of the acceptance period (the time in which creditors have to vote on the plan) and ends when the restructuring plan ends.[23]

The procedure is commenced by the debtor company's directors appointing a 'restructuring professional' by resolution of the board.[24] The restructuring practitioner must be a registered company liquidator.[25] The primary role of the restructuring practitioner is to assist with the formulation of the restructuring plan by the directors of the debtor company, certify the documents to be provided to creditors and then arrange for the creditors to vote on the plan.[26] The restructuring practitioner also has a role approving transactions that may be outside of the ordinary course of the company's business.[27]

Prior to voting on the restructuring plan, the company operates 'in restructuring', which confers protection for enforcement action taken against the company, its property or property that it is using.[28] These protections are very similar to the protections given to companies in voluntary

17 *Corporations Act 2001* (Cth) s 453A ('*Corporations Act*'); *Corporations Regulations 2001* (Cth) reg 5.3B.02 ('*Corporations Regulations*').
18 *Corporations Regulations* (n 17) reg 5.3B.17 (definition of 'proposal period').
19 Ibid regs 5.3B.17(2), (4).
20 Ibid reg 5.3B.21(3).
21 Ibid regs 5.3B.02, 5.3B.20 (lapsing of restructuring plan).
22 The company is no longer under restructuring once its restructuring plan is approved by the creditors during the acceptance phase: ibid reg 5.3B.02(1)(j).
23 Ibid regs 5.3B.21, 5.3B.25. The restructuring plan ends when one of the events in *Corporations Regulations* (n 17) reg 5.3B.02 occurs.
24 *Corporations Act* (n 17) s 453A(a).
25 Ibid s 456B.
26 Ibid s 453E; *Corporations Regulations* (n 17) regs 5.3B.21, 5.3B.37.
27 *Corporations Act* (n 17) s 453L(2)(b); *Corporations Regulations* (n 17) regs 5.3B.04–5.3B.05.
28 *Corporations Act* (n 17) ss 453R–453S.

administration,[29] with exceptions for conduct with the consent of the restructuring practitioner or with leave of the court. There is a stay against seeking a winding up of the company by the court.[30] However, this does not extend to suspending the right of the company's directors to propose a voluntary liquidation to the members.[31] This may be contrasted with pt 5.3A, where the directors' management power is suspended.[32]

Secured creditors' rights are largely suspended (as they are in pt 5.3A), with secured creditors holding security over the whole, or substantially the whole, of the company's property maintaining limited enforcement rights during the decision period.[33] Part 5.3B also includes identical ipso facto protections to those that exist in pt 5.3A.[34] This is unfortunate, given the varied and complex exceptions that exist for the ipso facto protections,[35] which may increase the cost and complexity of restructuring under pt 5.3B for MSMEs, particularly as the directors will need to address any asserted exceptions to ipso facto protections, most likely by seeking advice from the restructuring practitioner and lawyers. The restructuring practitioner has the power to dispose of encumbered property provided that it is in the ordinary course of the company's business or with the consent of the secured party, owner or lessor or with the leave of the court.[36] The court may make orders limiting the rights of secured creditors, owners or lessors, provided that their interests will be adequately protected.[37]

As one can see, the procedures in pt 5.3B have similarities with pt 5.3A but with less reporting obligations and no creditor meetings. The company is deemed to be insolvent if restructuring plan is put to creditors and the company can choose to appoint an administrator or move to liquidation at any time.

IV The concerns that Australia now has a maladroit system for corporate MSMEs insolvency

Arguably the new procedure is not sufficiently simple or streamlined as suggested by the explanatory material and this means that it will be costly for companies, risky for practitioners and potentially unrewarding for creditors to be involved. No doubt there will be many aspects of the new law that will be clarified by the courts in due course but some concerns that are glaringly obvious are discussed below.

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29 Ibid ss 440B, 440D.

30 Ibid s 453Q. See further *Re Dessco Pty Ltd* [2021] VSC 94; *Re DST Project Management and Construction Pty Ltd* [2021] VSC 108.

31 This would bring the period of restructuring to an end under *Corporations Regulations* (n 17) reg 5.3B.02(1)(g).

32 *Corporations Act* (n 17) s 198G.

33 Ibid s 454C (generally 13 business days from commencement).

34 Ibid pt 5.3B div 2 sub-div G.

35 See further Jason Harris and Christopher Symes, 'Be Careful What You Wish For! Evaluating the Ipso Facto Reforms' (2019) 34(1) *Australian Journal of Corporate Law* 84.

36 *Corporations Regulations* (n 17) reg 5.3B.39.

37 Ibid reg 5.3B.64.

A It is not debtor-in-possession ch 11-style corporate rescue

The new Part is described by the government as a debtor-in-possession regime where the directors of the company remain in control. There are several suggested benefits of this model. Firstly, the debtor-in-possession model may result in lower costs than external administration because there is no external administrator who has to run the business and whose work (and the work of their employees) has to be paid for, whereas existing management may draw lower fees or indeed may draw no wages if it gives the business a greater chance of survival. There are also lower investigation and reporting obligations imposed on the restructuring practitioner, who does not prepare a detailed report (as is required in pt 5.3A), but merely declares whether there are reasonable grounds to believe that the company is eligible to use the procedure and that it is likely to comply with the plan.[38] This could, in theory, lower the cost of the procedure, but the restructuring practitioner faces criminal sanctions if they fail to make reasonable inquiries into, and also verify, the company's business, property, affairs and financial circumstances.[39]

The notion that pt 5.3B is a debtor-in-possession procedure with the restructuring practitioner playing a hands-off is not consistent with the restrictions imposed on management decision-making and the likely need to request permission from the restructuring practitioner for a range of common tasks involved in running a business. While ordinary course of business limitations are common in foreign SME restructuring procedures, these limitations are broader than the new pt 5.3B because they rely on general law notions of the ordinary course of business, while the new procedure specifically carves out common business decisions from the ordinary course, thus requiring restructuring practitioner permission.

The agency role given to the restructuring practitioner also demonstrates a hybrid debtor-in-possession model, certainly not external administration as seen in pt 5.3A, but not the debtor-in-possession model seen in North America. Where savings may arise is in the lower reporting and investigation obligations compared with pt 5.3A. The restructuring practitioner is not required to prepare an investigatory report for creditors or to convene creditor meetings. However, these savings may not be fully realised because of the need to continually monitor the business in order to make decisions where permission of the restructuring practitioner is needed. The restructuring practitioner is also an officer of the company and is bound by statutory duties to act in the best interests of the company and with care and diligence. The restructuring practitioner also has potential criminal liability risk in relation to the declaration to creditors about the restructuring plan, where the restructuring practitioner must make reasonable inquiries into the company's business, property, affairs and financial circumstances and take reasonable steps to verify these details. If registered liquidators acting as restructuring practitioners see these obligations as involving detailed reviews, then the fixed fees for restructuring work will be higher than the government anticipates. If

38 Ibid reg 5.3B.18.
39 Ibid reg 5.3B.18(4).

restructuring practitioners see these obligations as perfunctory, and simply rely on information provided by the company's directors, then the utility of the declaration and ultimately of the new procedure itself will be undermined as will creditor confidence in the new system.

Secondly, the debtor-in-possession model may encourage earlier appointments by the company's directors because, unlike in pt 5.3A, they will not be ousted from management and will remain in control. This factor is likely to be of greater significance in MSME and family businesses where there is a sentimental attachment to the business continuing. However, with MSME directors often having personal guarantees over the company's debt and therefore a blending between the assets and liabilities of the business and the owners/directors, there is a strong economic disincentive to initiate an insolvency process until forced to do so by external factors, such as tax office enforcement against the directors. While there is protection against the enforcement of personal guarantees,[40] this is only for the restructuring period (approximately 3 weeks) and no protection for the period of the restructuring plan (which can last for up to 3 years).[41] Furthermore, the emotional connection that many small business owners have to their business may inhibit early appointments, because doing so may admit that they have failed.

Thirdly, the debtor-in-possession model may provide greater flexibility because there are fewer tasks for the restructuring practitioner to do than a voluntary administrator has to comply with (such as creditor meetings and notices to various stakeholders) under pt 5.3A.

Finally, the debtor-in-possession model may address the stigma attached to a business entering external administration. Keeping the existing management in place reduces disruption for the company's stakeholders and may reduce the perception of failure. However, for MSMEs, the financial difficulties that led to the appointment of the restructuring practitioner may mean that creditor distrust of management already exists and retaining management may not benefit from the restructuring effort. One of the benefits of voluntary administration in pt 5.3A is to have the administrator as a circuit breaker for the relationship between the company and its creditors.

B Incomplete information for the creditors

Part 5.3B requires the company to provide the restructuring plan (for voting on by the creditors) and a restructuring proposal statement.[42] The restructuring plan may include information relating to the company's financial affairs and must set out what property of the company is to be dealt with under the plan, but need not otherwise disclose the assets of the company or other financial

40 *Corporations Act* (n 17) s 453W.

41 *Corporations Regulations* (n 17) reg 5.3B.15(4)(b). Several submissions to Treasury during the consultation period pointed out that this would be a problem for MSMEs using the new laws: see, eg, Chartered Accountants Australia and New Zealand, Submission to Treasury, *Insolvency Reforms to Support Small Business: Corporations Amendment (Corporate Insolvency Reforms) Bill 2020* (12 October 2020); Australian Restructuring Insolvency and Turnaround Association, Submission to Treasury, *Insolvency Reforms to Support Small Business* (12 October 2020).

42 *Corporations Regulations* (n 17) reg 5.3B.14(1).

matters.[43] The restructuring proposal statement must include the schedule of debts and claims, but this also does not disclose the assets of the company.[44] There is no limit on the assets of companies that may use the procedure, so creditors could be presented with an incomplete picture of the company's financial position when being asked to vote, without an opportunity for a meeting to discuss the issues. Of course, it could be argued that, in the face of incomplete information, the creditors may simply vote against the plan or refuse to vote at all, but that seems an inadequate policy response to simply suggest that the new procedure not be used if creditors are unhappy with the levels of disclosure provided. Furthermore, the restructuring practitioner is not required to report on the commercial value of the proposal, or to advise creditors whether it would be in their best interests to approve or reject the plan. The restructuring practitioner is merely required to declare whether they believe on reasonable grounds that the company satisfied the eligibility criteria, whether all required information has been provided and whether the company is likely to be able to discharge its obligations under the restructuring plan.[45]

The restructuring practitioner is required to make reasonable inquiries into the company's business, property, affairs and financial circumstances and to verify these matters,[46] but there is no requirement for a general report to creditors (or to the court) to be provided to explain the nature of the procedure, or the creditors' other options if the plan is not approved.

The apparent rationale for this minimal level of reporting is to keep the costs of the new procedure down, but this stands in contrast to the requirement to seek approval from the restructuring practitioner for a large range of decisions (classified as not 'in the ordinary course of business') affecting the day-to-day running of the business.[47] The restructuring practitioner is able to terminate the restructuring period if they believe that the restructuring plan would not be in the interests of creditors.[48] It is curious that the role of the restructuring practitioner is not more closely aligned with the interests of creditors. The restructuring practitioner is an officer of the company and owes no specific duty to act in the best interests of creditors.[49]

There is a lack of information provided to creditors, at least compared with pt 5.3A, and this is understandable given the stated purpose of the new pt 5.3B is not to save the company or any part of its business, but merely to enable companies to retain control of the business while they develop a restructuring plan and to enter into a restructuring plan with creditors.[50] The goal is not

43 Ibid reg 5.3B.15.
44 Ibid reg 5.3B.16.
45 Ibid reg 5.3B.18.
46 Ibid reg 5.3B.18(5).
47 *Corporations Act* (n 17) s 453L; ibid reg 5.3B.04.
48 *Corporations Act* (n 17) s 453J(1).
49 Ibid s 9 (definition of 'officer'), s 181; Andrew Keay, *Company Directors' Responsibilities to Creditors* (Routledge-Cavendish, 2007); Anil Hargovan and Jason Harris, 'For Whom the Bell Tolls: Directors' Duties to Creditors after *Bell*' (2013) 35(2) *Sydney Law Review* 433. Even the power to terminate the restructuring if it is not in the interests of creditors is only expressed as a discretion (the restructuring practitioner may terminate) and not a duty to do so.
50 *Corporations Act* (n 17) s 452A.

necessarily to rescue the company in distress, but simply to present a deal (in the form of a restructuring plan) to the creditors. The restructuring practitioner does not report on whether the company will be rescued by the restructuring plan but merely whether there are reasonable grounds to believe that the company can comply with its terms.[51]

It may be argued that the minimal information provided to creditors leaves it open to creditors to be more proactive and request what information they want before making a vote on the restructuring plan, adopting an approach of 'you snooze, you lose'. However, the new pt 5.3B does not allow creditor meetings, which is the primary forum where creditors can express their concerns to the administrator — the creditors merely have the option to vote on the restructuring plan put by directors.[52]

C Incentive misalignment

The new pt 5.3B arguably contains few incentives for existing management to use the procedure, risk and questionable compensation for registered liquidators to act as restructuring practitioners and a confused set of incentives for creditors.

1 For the company and its directors

There appears to be a lack of strong incentives for the company's directors to use the new restructuring procedure. While getting a restructuring plan approved might provide financial relief for the company, the new procedure offers much less flexibility than pt 5.3A and has some features that will be disadvantageous for directors.

It is common for MSMEs to rely upon finance from the directors and shareholders, who are usually owner/managers. The new pt 5.3B treats directors and members as 'excluded creditors' because they are 'related creditors'[53] and voting by excluded creditors on the restructuring plan must be disregarded.[54] This means the person(s) who may well be the largest single creditor to the company, but who are also directors and members, are not permitted to vote on its future. There is no similar limitation for other forms of external administration.

While the restructuring period provides protection against the enforcement of personal guarantees given by directors and relatives of directors,[55] that protection will end once the company moves into a restructuring plan. This may mean that creditors holding guarantees can make the director or related party bankrupt if they can't satisfy the guaranteed debt. The guaranteed debts cannot be included in the terms of the restructuring plan because they are not an admissible debt or claim.[56] One positive aspect of the new pt 5.3B for

51 *Corporations Regulations* (n 17) reg 5.3B.18(2)(a)(ii).
52 Ibid regs 5.3B.21, 5.3B.25.
53 Ibid reg 5.3B.01.
54 Ibid reg 5.3B.25(2)(c).
55 *Corporations Act* (n 17) s 453W.
56 *Corporations Regulations* (n 17) reg 5.3B.01.

directors is that entry into restructuring will provide potential relief from director penalty notices under tax administration laws.[57]

There are also limits on what a restructuring plan is able to achieve that will hinder its utility for addressing MSME debt problems. The restructuring plan must be a cash payment as a dividend (so no debt/equity swaps or in specie distributions),[58] and all creditors must rank equally.[59] This means that directors or related parties who are also creditors must be paid the same rate of dividend as unrelated creditors. The requirement to pay pari passu is a standard term that must be included in all restructuring plans and can't be waived or varied.[60]

Crucial to the operation of pt 5.3B is the 'eligibility criteria' and this is defined to include that the company will have liabilities of less than $1 million.[61] Additionally, no director (or former director in the last 12 months) has been a director of a company that has used restructuring or the new simple liquidation within 7 years prior and that all of the company's employee entitlements that are due and payable must be paid before putting a plan to creditors.[62] Furthermore, the company's lodgment of tax needs to be up to date.[63] The requirement to have tax lodgments up to date and all employee entitlements to be due and payable before a restructuring plan is put to the creditors will mean that many/most MSMEs will be unable to use the new procedure as levels of compliance in that sector are notoriously low.

2 For creditors

The new pt 5.3B seems aimed at simply presenting a restructuring plan to creditors, rather than formulating a sustainable restructuring plan that is in the best interests of creditors. The lack of detailed information being provided to creditors will not engender confidence within the creditor body. The parliamentary intention of keeping the reporting and investigations to a minimum, as well as the debtor-in-possession rather than the external administration model, supposedly to keep the costs down, is not supported by the number and complexity of the provisions being inserted into the *Corporations Act*, *Corporations Regulations 2001* (Cth) ('*Corporations Regulations*') and *Insolvency Practice Rules (Corporations) 2016* (Cth) (which are much longer than for pt 5.3A). The new procedure for voting,[64] using a novel schedule of debts and claims determined by the directors[65] and then leaving it up to creditors to challenge the assessment,[66] will also lead to confusion within the creditor body and no doubt disputes about the directors' assessment. The process for resolving such disputes is also cumbersome,

57 *Taxation Administration Act 1953* (Cth) s 269-15(2)(ba).
58 *Corporations Regulations* (n 17) reg 5.3B.15(4)(a).
59 Ibid regs 5.3B.27(1)(a)–(b).
60 Ibid reg 5.3B.27(2).
61 *Corporations Act* (n 17) s 453C; ibid reg 5.3B.03.
62 *Corporations Act* (n 17) s 453C; *Corporations Regulations* (n 17) regs 5.3B.03, 5.3B.24.
63 *Corporations Regulations* (n 17) reg 5.3B.24.
64 Ibid reg 5.3B.25.
65 This is included as part of the 'restructuring proposal statement', which is given to creditors: ibid reg 5.3B.16.
66 Ibid regs 5.3B.22–5.3B.23.

including the potential for multiple rounds of creditor voting,[67] and will result in multiple pieces of correspondence between the restructuring practitioner and the creditors and variations to the proposed payments under the restructuring plan. The uncertainty this causes is likely to incentivise restructuring practitioners to increase their level of up-front fees, as only litigation allows for variable fees to be charged for the restructuring period.[68]

The voting mechanism is also highly problematic because it is based only on a simple majority in value of the creditors who respond to the restructuring practitioner's notice requesting voting, meaning that a small number of creditors could approve of the restructuring plan.[69] This may mean that large creditors, such as the Commissioner of Taxation, have effective control over the plans because they will usually be the single largest unsecured creditor who is eligible to vote. In other forms of insolvency administrations, the voting threshold always includes both majority in number and value.[70]

The new pt 5.3B is modelled on voluntary administration, but there are significant differences that are averse to the interests of creditors. Principally, the fact that the restructuring practitioner is not managing the company means that they do not have the same personal liability that voluntary and deed administrators have.[71] This is problematic because it means that creditors who continue dealing with the company during the period of restructuring will not be assured of payment, as they are during pt 5.3A (because of the administrator's personal liability). This is likely to lead to creditors insisting on pre-payment or cash on delivery, which may further constrain the company's cash resources. There is also a risk for creditors that if the company enters liquidation, then payments made to creditors during the period of restructuring (or during a restructuring plan) will be claimed as unfair preferences.[72] It should be noted, however, that this is also a risk for transactions during a deed of company arrangement under voluntary administration.[73]

The circumstances that follow the termination of restructuring or the failure of a restructuring proposal are also problematic for creditors, when compared with the position under voluntary administration. Where a period of administration ends, the company will usually automatically transition to a creditors' voluntary liquidation.[74] However, there is no automatic transition from pt 5.3B to a creditors' voluntary liquidation, with the position left to the directors to consider whether they wish to continue trading (which may involve the risk of insolvent trading) or seek to appoint an external administrator. The failure of a vote on the restructuring plan will bring the period of restructuring to an end.[75] The court could use its general power under

67 Ibid.
68 *Insolvency Practice Rules (Corporations) 2016* (Cth) r 60-1B ('*Insolvency Practice Rules*').
69 *Corporations Regulations* (n 17) regs 5.3B.21, 5.3B.25.
70 *Insolvency Practice Rules* (n 68) r 75-115.
71 Such as liabilities for debts incurred during the restructuring period. Cf during voluntary administration: *Corporations Act* (n 17) ss 443A–443B.
72 Ibid ss 588FA, 588FC, 588FE(2C), 588FF.
73 Ibid ss 588FE(2A)–(2B).
74 Ibid ss 446A–446AA.
75 *Corporations Regulations* (n 17) regs 5.3B.02(1)(c), 5.3B.20.

s 458A to terminate the restructuring and appoint a liquidator. It is curious that the restructuring practitioner and the creditors lack the power to terminate a restructuring plan, unlike in pt 5.3A.[76] The *Corporations Regulations* provide for a plan approved by creditors to be terminated by a court order or by a breach of the terms that lasts for 30 business days without being rectified.[77] It is open for the restructuring practitioner to seek a court order to terminate the plan.[78] The reliance on court orders to terminate a plan is particularly troubling in circumstances where the creditor vote to approve of the restructuring plan does not require a majority of the creditors to approve the plan. This is a further reason that the new procedure is unlikely to offer lower cost savings or to engender creditor confidence as voluntary administration does.

3 For the restructuring practitioner

The new pt 5.3B requires fixed fee arrangements for the restructuring practitioners to be determined by the commencement date of the procedure[79] and requires a percentage of dividend distributions to be used at the method for calculating remuneration under a restructuring plan.[80] The restructuring practitioner also has potential criminal liability if they do not undertake reasonable endeavours to investigate and verify the company's business property and affairs,[81] despite (supposedly) not being in a management role. It is uncertain as to what level of detail will be needed to satisfy this requirement. With so much uncertainty involved in the new procedure and the modified debtor-in-possession model chosen where the restructuring practitioner is likely to be asked to make many management decisions for the debtor company, these remuneration requirements seem unduly restrictive and are likely to result in higher charging practices to account for that risk and uncertainty.

V Conclusion

The federal government's move to introduce a debt restructuring law for corporate MSMEs is understandable given how badly they have been affected by the COVID-19 pandemic and the lobbying on behalf of this sized company that they be provided with relief beyond what exists in pt 5.3A. However, as this update shows, there are broad concerns that the new Part will not be embraced as the reform falls short in a number of key areas for debtors, creditors and the professionals who are expected to recommend and then implement it.

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76 Cf *Corporations Act* (n 17) s 445E.
77 *Corporations Regulations* (n 17) reg 5.3B.31.
78 *Corporations Act* (n 17) s 458A, sch 2 s 90-15.
79 *Insolvency Practice Rules* (n 68) r 60-1B.
80 Ibid r 60-1C.
81 *Corporations Regulations* (n 17) regs 5.3B.18(4)–(5).