

The Manager, Corporations and Schemes Unit
Financial Systems Division
The Treasury
Lamgton Crescent
PARKES ACT 2600

Via email: insolvency@treasury.gov.au

Dear Sir/Madam

In April 2016 the Australian Government issued a Proposals Paper titled *Improving Bankruptcy and Insolvency Laws (Proposals Paper)* and sought feedback for the public. Fox Symes welcomes the opportunity to do so.

Fox Symes is the largest provider of personal insolvency solutions in Australia and over the past 16 years we have assisted tens of thousands of Australians to address their unmanageable debt through a range of solutions which include bankruptcy, personal insolvency agreements and debt agreements. We are therefore well placed to comment particularly on the proposed amendments to the *Bankruptcy Act 1966 (the Act)*.

SUMMARY

The Proposals Paper concluded that changes to insolvency laws would encourage entrepreneurship and innovation which it argued is constrained because of the existing laws. Any initiative or public policy which encourages and fosters innovation and the entrepreneurial spirit should be applauded and endorsed because this will lead to job creation and national prosperity.

The key recommendations of the Proposals Paper are to:

1. Reduce the current default bankruptcy period from three years to one year
2. Introduce a “safe harbour” for directors from personal liability for insolvent trading if they appoint a restructuring advisor to develop a turnaround plan for the company, and
3. Make “ipso facto” clauses, which have the purpose of making contracts to be terminated solely due to an insolvency event, unenforceable if a company is undertaking a restructure.

While these proposals appear to be simple and straightforward and if implemented may result in a preparedness and willingness for entrepreneurs to “*embrace risk, learn from mistakes, be ambitious and experiment to find solutions*” there are many areas it does not address and because of this we have questions which require answers. Critical to any reform is the need to ensure that whatever changes are implemented that they achieve their objective and do not

encourage a greater number of debtors to file for bankruptcy because it is an “*easy way out*”. Having said that Fox Symes supports insolvency reforms that:

- Encourages entrepreneurship
- Protects against an abuse of the bankruptcy laws
- Ensures that any debtor faced with an insolvency event, either consumer or business, has options to choose from which are fair, viable and different
- **Rewards and recognises debtors who elect to repay their debts rather than filing for bankruptcy** which the Proposals Paper fails to address
- Strikes a balance which encourages entrepreneurship while not encouraging the abdication of individual responsibility for financial decisions
- Does not make bankruptcy the “easy way out”
- Are the outcome of a robust and rigorous review and an extensive and thorough public consultation process.

Will a one year bankruptcy term lead to entrepreneurship?

Over past decades successive Governments have made various amendments to the Act with the purpose and intention of "*encouraging debtors to seriously consider using alternatives to bankruptcy where possible*" and to ensure that bankruptcy was "*less an easy option*" and to "*make it harder for people to abuse Australia's bankruptcy system*". Significantly the prevailing message conveyed by AFSA is that bankruptcy must be viewed as "*the last resort*".

The amendments to the Act were prompted by an increase in bankruptcy when credit availability significantly increased. Access to consumer credit has not diminished in fact there is an evolution in the types of consumer credit available and consumer debt levels continue to rise during a period of record low interest rates.

Data provided by AFSA states that business related bankruptcies have declined over past years and that the majority of bankrupts are non-business related, low income earners without assets.

We are therefore perplexed as to what evidence or facts were relied upon to assume that a reduction in the bankruptcy period from three to one year would stimulate or lead to entrepreneurial behaviour? If there is concrete evidence to support this assumption we suggest it be made public.

Over the last sixteen years we have assisted tens of thousands of Australians who were dealing with unmanageable debt. The vast majority of these were in debt because of consumer consumption supported by easy access to credit. From our experience we have seen little evidence to suggest that the proposal to reduce the bankruptcy term from three to one year will result in and encourage entrepreneurship.

Despite this we recognise that there is validity in reducing the bankruptcy term to one year. The majority of bankruptcy administrations are non-business related low income earners without assets termed “consumer bankruptcy” and they do not yield a return to creditors. We therefore see an economic imperative and reason to implement this measure. However it is imperative to contemplate how a reduction in the bankruptcy term to one year may unleash

an increase in debtors filing for bankruptcy to avoid paying their debts especially if there is a corresponding reduction in the retention period for personal insolvency information in credit reports thus enabling a discharged bankrupt access to fresh credit.

Access to credit

The Proposals Paper raises the query as to whether it is appropriate to reduce the retention period for personal insolvency information in credit reports. Even though a time frame is not indicated, it could be assumed that the intention was to align the retention period with the one year bankruptcy discharge period.

In 2009 the Government enacted the NCCP Act to protect consumers from predatory credit activities. A key component of this legislation was the introduction of the responsible lending provisions of the NCCP thus ensuring ethical and profession standards were applied and complied with across the finance industry.

This leads to questioning the wisdom of creating an environment which allows a bankrupt discharged after one year, to immediately be able to access fresh credit especially given AFSA's statistics show that the one of the most common reasons debtors file for bankruptcy is excessive use of credit. To do so would contradict the statement on page three of the Proposals Paper which states that one of the intentions of the proposed measures was "*to encourage Australians to .. learn from mistakes*". It would not make any sense to tempt a discharged bankrupt to repeat their mistakes.

This measure could also undermine the objective articulated in the Proposals Paper of a striking a "*better balance between encouraging entrepreneurship and protecting creditors.*"

We repeat that the majority of people who enter into a formal insolvency agreement do so because of unmanageable consumer debt resulting from easy access to credit or from a change in their personal circumstances. Few are related to a failed business venture.

The "stigma" impact

The proposal paper states "*our current insolvency laws put too much focus on penalising and stigmatising the failures.*" We agree and suggest that any review of the Act should include a review of the other administrations under the Act and these are a debt agreement and a personal insolvency agreement. The Proposals Paper is silent regarding these.

Successive governments have encouraged and supported the use of alternatives to bankruptcy and debtors have responded positively to these alternatives, particularly the debt agreement option. Unlike most consumer bankrupts, debtors who elect to rely upon a debt agreement repay creditors a portion of their debts and creditors benefit more from a debt agreement than they do from bankruptcy. Despite this debtors who rely upon a debt agreement are treated by creditors as though they were bankrupt. A reason for this is because, although a debt agreement is an "*alternative to bankruptcy*" proposing a debt agreement or being party to a debt agreement is "*an act of bankruptcy*". As a consequence the credit report of a debtor who is party to a debt agreement has a notation "*act of bankruptcy*" listed on their report. Few creditors understand the difference between being a bankrupt and an "*act of bankruptcy*" and the debtor is presumed to be a bankrupt and stigmatised.

We therefore urge the Government to amend this provision of the Act to ensure that a debtor who elects to repay their debt through a debt agreement or a personal insolvency agreement be differentiated and not labelled as “bankrupt”. In fact their commitment to repaying their debt should be commended and they should not be “*stigmatised*” for doing so.

Creditors have played a key role in shaping out insolvency laws and they will continue to play a pivotal role influencing any future changes. We therefore pose a question to creditors. We would like them to explain why they so harshly judge and impose high and on occasion unrealistic demands for repayment/ returns on debtors who elect to make an arrangement to repay their debts rather than filing for bankruptcy? The arrangements include debt agreements, personal insolvency agreement, informal arrangements and hardship.

This raises the question of the “stigma” impact of our insolvency laws. From experience the “stigma” attached to bankruptcy or any formal insolvency remedy is not one “felt” by debtors; rather it is one “imposed” by creditors and there is no certainty or guarantee that a change in any law will result in a change in human behaviour and attitude.

Other considerations

Debtors need options other than bankruptcy.

A potential, or current, entrepreneur may be deterred from embracing risk or engaging in entrepreneurial endeavours because they have assets and they know that, should they be confronted with an insolvency event, they face losing them. By increasing the current thresholds for a debt agreement, and the thresholds apply to liabilities, income and net assets, more Australians may be encouraged to embrace risk and engage in entrepreneurial activity knowing that their assets are protected.

Ongoing obligations

Should the Government reduce the period of bankruptcy to one year to encourage entrepreneurial activity then the bankrupt’s obligations to assist the administration of their bankruptcy must remain. This should include the obligation to pay income contributions for three years if applicable.

It should be acknowledged that ensuring a discharged bankrupt co-operates with their Trustee may be a difficult and challenging task.

Overseas travel

We support the reduction of the overseas travel restriction to one year, subject to any extension for misconduct.

Conclusion

Fox Symes supports the Government’s initiative of investigating ways to drive prosperity by encouraging innovation and entrepreneurship. We agree that the current insolvency laws do put too much focus on penalising and stigmatising the failures, either consumer or business, and little if any recognition is given to those who do repay their debts through a debt agreement or personal insolvency agreement. Review and change is greatly needed and

overdue. Our primary concern is that this broad paper and the four week response period are inadequate to review, address and consult on these significant and fundamental changes. A robust and rigorous review and extensive public consultation is required.

We hope this submission will assist. Should you wish to discuss our comments please contact Deborah Southon (02) 8985 5091 or dsouthon@foxsymes.com.au

Yours sincerely
Fox Symes