25 February 2022

Senator the Hon Michaelia Cash
Attorney-General
Canberra ACT 2600

Via: Citizen Space survey

Bankruptcy system – options paper

Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia represent more than 300,000 professional accountants in over 100 countries around the globe. We make this joint submission to the '*Bankruptcy system – options paper*' on behalf of our members and in the broader public interest.

We concur with the Government's comment that stakeholder views on the merits of the Enterprise Incentives Bill (the Bill) remain largely unchanged. That is, that change is needed to address the stigma of bankruptcy and encourage entrepreneurship. We do not support the government's view that the changes proposed in the Bill remain fit for purpose. In particular, we do not support reducing the default period of bankruptcy to one year, noting that 83 per cent of previous submissions did not support such a reduction.

Accordingly, as indicated in our responses to the survey, we:

- do not support reducing the default period of bankruptcy to one year
- support strengthening the objection to discharge provision
- do not support strengthening offence provisions
- do not support extending the default term for debt agreements
- do not support increasing thresholds for debt agreements
- support expanding the information provided on pre-insolvency advisers
- do not support requiring registered trustees to undertake unfunded enquiries
- do not support new offences targeted at untrustworthy advisers as proposed.

We consider that the proposals in the current paper aimed at addressing concerns raised by stakeholders appear to contradict the government's own deregulation agenda. For example, in reducing the period of bankruptcy to one year, whilst simultaneously adding layers of conditions and exemptions, increases the potential number of periods of bankruptcy, thereby making an already complex framework more complex. By handling 80 per cent of bankruptcies and receiving data provided by registered trustees in annual administration returns (AAR) for the other 20 per cent, the Government is well placed to interrogate data to innovate and propose evidence based, value adding, change.

As the Government has concluded that it is too difficult to differentiate between a business related and a consumer driven bankruptcy, any change must consider the impact on reckless consumers—who build credit card debt with no intention of paying that debt—as well as the desire to encourage entrepreneurship, noting that entrepreneurs also need boundaries and consequences for their actions.

Critically, it is not the role of the *Bankruptcy Act 1966* (the Act) to determine what opportunities a person may have once out of bankruptcy. For example, in seeking credit it is the credit providers role to determine risk and offer credit at a price that accounts for such risk. It is the role of the Act to create a framework in which both debtors and creditors can determine the pathway they should follow to best address personal insolvency. That framework should be simple, easily understood by both debtors and creditors and able to be efficiently administered by the Official Trustee and registered trustees.

To address the stigma of bankruptcy and encourage entrepreneurship, it is the record of bankruptcy, not the period of bankruptcy, that should be addressed. The record for life on the National Personal Insolvency Index (NPII) is unique and out of line with other Government legislation. Accordingly, we recommend removing the public record from the NPII at the same time as the record is removed from credit reporting bureaus. We acknowledge that the Government may wish to keep a record in perpetuity to enable data analysis and the detection of repeat bankrupts, which we believe represent a tiny portion of bankrupts. Accordingly, whether the record is publicly available in perpetuity should be determined with consideration of the impact on the majority of, genuine, bankrupts wishing to have a clean slate to start again.

Measures to prevent repeat bankruptcy are absent from the proposals to address stakeholder concerns. The Government should require an element of education when people utilise any available pathway under the Act to manage personal debt. For example, these could include how to manage cash flow and raising awareness of what actions impact your credit rating.

We consider that the proposals increase complexity, will foster reckless and repeated bankruptcies and will fail to address the stigma of bankruptcy or encourage entrepreneurship. Change must seek a balance between fostering an innovative ecosystem with the damage caused to other participants in that ecosystem by reckless and repeat bankrupts. Attached is our detailed feedback to the proposals (Appendix A).

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Yours sincerely

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Appendix A

Reduce bankruptcy period to one year

The rationale for, and the purpose of, reducing the bankruptcy period to one year is unclear as the proposal also seeks to add layers of conditions and exemptions, increasing the possible periods of bankruptcy. This additional red tape will further complicate an already complex regime. Further complexity will prevent debtors from making an informed decision as to the best pathway to manage their personal debt. It will also inhibit creditors from working with debtors to extend credit during periods of economic uncertainty and increase the work, and therefore cost, for trustees to manage the estate of a bankrupt.

It is important for legislation to recognise that bankruptcy does not happen in a vacuum. Personal bankruptcy impacts credit providers, trade credit providers and family members. The Australian Financial Security Authority (AFSA) reports that for the September quarter 2020 of total debt owed, 35% was to banks and a further 32% to businesses, sole traders and individuals. Accordingly, change must consider the many steps in the process that creditors need to follow to commence the process to bankrupt an individual. These are significant and costly with fees to do so in the range of $5,000 to $10,000. If a bankruptcy petition on a creditors' application leads to a debtor only being made a bankrupt for one year, then many creditors would not go to the trouble of making a petition. Instead, they will simply not provide credit.

We note that the Act already provides for an early discharge mechanism as prescribed under Section 73. A debtor can seek this early discharge by way of a compromise on creditor debts. Further, we note that the Act has previously had an early discharge provision which we would recommend be revived. Such a provision, for example, would enable the bankrupt to be discharged from bankruptcy when a registered trustee completes and finalises the administration of the bankrupt estate with the Official Receiver, anytime within the three-year default period. This would help promote collaboration between the bankrupt and the trustee, should the bankrupt be motivated to be discharged prior to the default three-year period.

Strengthen objection to discharge provisions

We support, in principle, the proposal to strengthen objections to discharge provisions, in particular, the inclusion of Sections 77 et al and 80 of the Act. In line with our position on an early discharge mechanism, we support such a proposal where a bankrupt fails to co-operate, and that failure removes the option of a registered trustee applying for an early discharge.

Strengthen offence provisions

Irrespective of the bankruptcy period, we see no need to strengthen the offence provisions. The key to offence provisions is enforcement, not more provisions. We consider the existing offence provisions, if appropriately enforced, to be adequate.

Promote debt agreements

We do not support the proposals to extend the default period to five years or to increase eligibility thresholds. We acknowledge that there has been a decline in the use of debt agreements but consider this is in line with recent declines observed across the entire insolvency landscape.

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It is unclear how the Government has determined a need to improve access to, and minimise the consequences of, debt agreements. Accordingly, we believe that further data analysis should be undertaken of bankruptcies to determine how many would have met the thresholds for a debt agreement. Only if this represents a significant number should further analysis be undertaken to determine if a debt agreement was considered and why it was subsequently discarded.

We urge the government to utilise existing data to undertake a thorough analysis of trends. The reduction in debt agreements may have been due to the Omnibus Package in 2020 or to better regulation.

Extend the default term

We question the reasoning behind why the Government considers that a debtor who cannot pay their contributions to their debt agreement in three years, would be able to do so within a five-year period. Further, there does not appear to be any analysis on the impact of creditors accepting smaller periodic payments over five years than accepting a potentially lesser amount over three years. For example, one impact to consider is the cost to a creditor to take on more debt to fill the gaps in cash flow or capital created by a debtor with a payback period of five years.

Increase thresholds

Noting that the latest average weekly earnings reported by the Australian Bureau of Statistics is $1,209, which indicates an average annual income of $62,868, the current income threshold of $90,772 would not appear to be a barrier to accessing debt agreements. Again, we suggest that the Government undertakes further analysis of the bankruptcy data already held to quantify the average value of debt and the pool of assets of a bankrupt, to determine if the current thresholds are a barrier to access. If not, it would suggest other factors determine the most appropriate pathway to manage personal insolvency, such as the complexity of the estate or the composition of creditors.
We would also caution against driving bankrupts into debt agreements without such analysis. We note debt agreement administrators are not required to have the skills and experience of a registered trustee in bankruptcy and are not as highly regulated. This reflects the purpose of debt agreements, which is to quickly deal with low value personal insolvencies. Where a personal insolvency involves complex arrangements and significant debt, the skills and experience of the Official Trustee or registered trustee in bankruptcy are required.

Target untrustworthy advisors

We support expanding the information on pre-insolvency advisers as currently captured in a bankrupt's Statement of Affairs. Currently, bankrupts simply indicate if they have received such advice. This could be expanded to record the name of the individual and/or firm that provided this advice.

We do not support requiring additional regulatory work by registered trustees to undertake enquiries to determine the pre-insolvency advice given. We consider such enquires, in essence investigations, are the work of AFSA, Australian Securities and Investments Commission (ASIC) and the Australian Taxation Office through the anti-phoenix taskforce.

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Pursuant to Section 19 of the Act and Division 42 of the Insolvency Practice Rules (Bankruptcy) 2016, where a registered trustee or bankrupt raises concerns about the person who provided pre-insolvency advice, the Official Receiver is best resourced to meet the burden of evidence to prosecute such a case. This work is already being undertaken as reported in AFSA's 2020-21 Annual Report, which notes that AFSA sources information on pre-insolvency advice and undertakes analysis to identify individuals and businesses who appear to be engaging in activities that intentionally misrepresent or avoid disclosing information regarding the debtor's financial affairs and prosecute.

We consider that the anti-phoenix taskforce has the skills and resources to detect, investigate and enforce compliance, or prosecute non-compliance, with the relevant legislation, such as *Corporations Act 2001* in respect of for providing financial advice.
Our position takes into consideration that the Official Trustee administers over 80 per cent of all bankruptcies and receives all the reports from estates administered by registered trustees. With the view that an untrustworthy adviser may advise, say, 20 people facing insolvency with each of these going to a different registered trustee to administer what remains in their estate, it is only the Official Trustee who would be able to detect the common pre-insolvency adviser.

Accordingly, it is the Official Trustee who can analyse and connect data, such as looking back to the pre-insolvency adviser disclosed by a bankrupt when possible breaches of the Act are identified by trustees.

Finally, we consider asking registered trustees to take on the role of a regulator by completing unfunded enquiries may breach the Inspector-Generals' Bankruptcy principles, which underlay section 42-60 of the Rules – Standards for Trustees, that

> In conducting an administration, a trustee must:
>
> - incur only those costs that are necessary and reasonable
> - before deciding whether it is appropriate to incur a cost, compare the amount of the cost likely to be incurred with the value and complexity of the administration
> - consider the views of creditors in relation to whether money held by the trustee should be applied to conduct further investigations in relation to the administration or distributed as a dividend.[42]

There is no utility in legislating further requirements on a registered trustee when those who are deemed to be untrustworthy can be prosecuted through existing legislation. Should the expertise of a registered trustee be required to assist in the investigation on behalf of the Official Receiver, this should be adequately funded similar to ASICs ability to utilise its assetless administration fund to appoint a liquidator to a company ASIC has ordered be wound up. Otherwise, the role of the registered trustee is to manage a bankruptcy and achieve the best outcome for creditors and the bankrupt.

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