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# Introduction of Code of Professional Practice by IPA

As most will be aware, the Insolvency Practitioners Association has introduced a comprehensive Code of Professional Practice.

The Code was launched at the recent national conference by Justice Austin.

The Code is something with which all Insolvency Practitioners and Stake Holders in the Insolvency profession must become familiar.

While there are many issues within the code, some of which will be discussed in future updates, one that is likely to be of immediate significance is the guidelines relating to independence. The introduction of these guidelines follows upon the recent amendments to the Corporations Act in relation to declarations of indemnities and relevant relationships.

The Code is likely to be a document to which the regulators and the Courts will give great weight when considering issues of professional conduct.

In particular, the guidelines relating to independence are something that all practitioners need to be very conscious of.

The test of independence as set out in the Code is that a practitioner **MUST** be independent in fact and be seen or perceived to be independent.

The issue of perception of independence is something that on occasions is likely to require very fine judgment. An obligation

is imposed upon the practitioner to be proactive in anticipating, identifying and uncovering the circumstances that may give rise to a conflict of interest.

There is a requirement that every firm must document and implement policies and processes to emphasise the importance of independence and to establish clear criteria and methods to identify and deal with any threats to independence.

This requirement emphasises the essential need for all firms to have effective compliance procedures in place.

The guidelines make it clear that a mere disclosure of an interest or a relationship that creates a lack of independence or the perception of a lack of independence does not remedy or cure the situation. The obligation to maintain independence remains upon the practitioner notwithstanding any such disclosure.

The introduction of this Code is something to be welcomed by the profession generally. Well-run firms with appropriate compliance procedures will have no difficulty in fully complying with the Code.

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# House of Lords addresses cross-border insolvencies

In *McGrath & Ors v Riddell & Ors* [2008] UKHL 21 the English House of Lords considered whether the English assets of four Australian HIH Group companies should be remitted to the Australian Liquidators.

## Facts

In the insolvent liquidation of four Australian HIH companies, the Supreme Court of New South Wales issued a letter of request to the High Court in London asking that the English provisional liquidators, be directed to remit the assets (mostly reinsurance claims) that were situated in England (after payment of their expenses) to the Australian liquidators for distribution. The question was whether the High Court should exercise their discretion and order that the assets should in principle be remitted to the Australian liquidators for distribution in accordance with the Australian statutory scheme or be retained in England and distributed in accordance with the English statutory scheme.

The Supreme Court of New South Wales made the request as a “relevant country” for assistance, pursuant to section 426(4) of the Insolvency Act 1986 (UK) which provides that the English Court “shall assist the Courts having the corresponding jurisdiction in any other part of the UK or any other relevant country or territory”.

In Australia, an insurance company’s assets are applied first to Australian debts and reinsurance proceeds are applied to the reinsured liabilities, whereas under the English statutory scheme at that time, those assets would be distributed *pari passu* among insurance, reinsurance and other unsecured creditors ie. the reinsurance creditors were a class of preferential creditors who would not have had priority under English insolvency law. If the assets were remitted, the result would be that some English creditors would lose out.

The English Court of Appeal held that the Court had jurisdiction, but that it should not be exercised because the outcome for some creditors would be worse than if the English assets were distributed according to English law.

## The decision

The House of Lords decided that the English assets should be remitted to Australia.

Lord Hoffmann (with Lord Walker agreeing) considered that it would not offend against any principle of justice for the assets to be remitted to Australia [at para 31] and that the application of Australian law to the distribution of all of the assets is more likely to give effect to the expectations of creditors as a whole than the distribution of some of the assets according to English law [at para 33].

There were also no grounds of justice or policy which required the English Court to insist upon distributing an Australian company’s assets according to its own system of priorities only because they happen to have been situated in England at the time of the appointment of the provisional liquidators. Lord Scott commented that to rely simply on the fact that under the insolvency scheme applicable to the principal winding-up, there would be a significant class or classes of preferential creditors whose debt would not have priority under the English insolvency scheme “was not sufficient to justify a refusal” [at para 52]. It was Lord Scott’s opinion that there was nothing unacceptably discriminatory or otherwise contrary to public policy in the Australian statutory provisions.

## Modified Universalism

An interesting aspect of the judgment is the fact that the Law Lords were divided on whether it was English common law or judicial principles, or Section 426 of the Insolvency Act, that allowed the result.

Lord Hoffmann did not base his decision on Section 426, but on an inherent jurisdiction of the English Courts. Lord Hoffmann referred to what English judges have for many years regarded as a general principle of private international law, namely that bankruptcy (whether personal or corporate) should be unitary and universal. “There should be a unitary bankruptcy proceeding in the Court of the bankrupt’s domicile which receives worldwide recognition and it should apply universally to all of the bankrupt’s assets” [at para 6].

Lord Hoffmann stated that the primary rule of private international law that applied in this case was the principle of (modified) universalism, which has been “the golden thread running through English cross-border insolvency law since the eighteenth century. That principle requires that English Courts should, so far as is consistent with justice and UK public policy, co-operate with the Courts in the country of the principal liquidation to ensure that all the company’s assets are distributed to creditors under a single system of distribution” [at para 30].

Lord Walker expressed himself to be in full agreement with Lord Hoffmann. However Lords Scott and Neuberger disagreed with Lord Hoffman’s reasoning but not his conclusion. Lord Scott accepted, as a general proposition, that there should be one universally applicable scheme

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of distribution of the assets of an insolvent company. However, Lord Scott stated that there is a potential conflict between the desirability of that general proposition, and the undesirability of a degree of confusion “coupled with the obligation of English Courts to accord to claimant creditors in an English winding up the statutory rights to which they are entitled under English insolvency statutes [at para 61]”. In Lord Scott’s view, this conflict was resolved by Parliament enacting section 426 in relation to “relevant countries” of which Australia was one.

### Conclusion

The judgment raises the relevance or applicability of a common law principle that Lord Hoffmann described as “modified universalism”. The decision is significant in the context of the increasing international legislative and judicial activity in the area of cross-border Insolvency Law.

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# Revised Guidelines for the Assetless Administration Fund

A liquidator is not obliged to incur the expense of fully investigating a company’s failure (over and above the minimum statutory requirements for reporting to ASIC and creditors) where the company does not have the assets or property to fund the expense of doing so (section 545 of the Corporations Act 2001 (Cth) (“Act”).

The Assetless Administration Fund (“AAF”) was created to address the perceived “regulatory gap” that arose when an assetless company was either not wound up, or was wound up but the circumstances of the company’s insolvency were not fully investigated, due to a lack of funds. The AAF aimed to address this by providing funds to facilitate more comprehensive investigation and reporting by liquidators into assetless companies where ASIC might commence proceedings to ban directors under s206F of the Act or in respect of “other matters”, such as breach of directors duties or insolvent trading.

The AAF was also established to deter phoenix activity, in which the assets of a failed entity are depleted and transferred into a phoenix company, often leaving insufficient assets to warrant the appointment of an insolvency practitioner.

From February 2006 to March 2008, the AAF had been underutilised, given the total available funding, as compared with the number of applications and consequent proceedings brought under the AAF. The initial criteria for funding under the AAF, may have inadvertently operated to deter or exclude potential applications because the funding available to a liquidator was limited to \$5,500 (incl GST), and because the test for whether a company was “assetless” took account of realisation costs incurred by third parties such as auctioneer and valuation costs.

In January 2008, the AAF funding criteria were amended (ASIC Regulatory Guide 109 (“Guidelines”). The amount

ASIC can pay a liquidator for a report prepared for a director banning order under s206F has been increased to \$8,250 (incl GST). Also a new definition of “assetless” has been incorporated to include both liquidations where there is less than \$10,000 in net realisable assets (Category 1), and liquidations where some work has been undertaken resulting in less than \$10,000 in net realisable assets after outlays for liquidator’s remuneration and other costs incurred, which are not directly related towards third party realisation costs (Category 2). The Guidelines also include further guidance for liquidators when submitting applications for funding to the AAF.

Consistent with ASIC’s suggestions, we recommend the following:

- (a) Consideration should be given to the AAF in each liquidation where there are limited funds;
- (b) The assistance of ASIC through the Liquidator Assistance Program should be sought if reports as to affairs are not completed. ASIC’s preference is for the availability of books and records to be determined before granting AAF funding, as necessary evidence may not be available if there are insufficient records.
- (c) Existing liquidations that fell outside the previous guidelines should be reviewed to determine if they are now eligible under the Guidelines.

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# In Brief

## Deputy Commissioner of Taxation v Meredith [2007] NSWSCA 354

- The Commissioner of Taxation issued a director penalty notice (under section 222AOE of the Income Tax Assessment Act 1936 (Cth)) for an amount equal to the amount of tax withheld from the salary entitlements of employees that had not been remitted to the Commissioner. The Commissioner was required to issue the notice at least 14 days before commencing proceedings to recover the amount of the penalty. By way of defence in the District Court, the taxpayer stated that she had not received the notice and was therefore not liable. The District Court found on the balance of probabilities that the notice had not been delivered.
- The Court of Appeal held that section 222AOF provides for a method of service of a director penalty notice and if that procedure is followed, then service is deemed effected and cannot be rebutted by evidence of non-receipt or non-delivery. The effect of the decision is that service will be deemed to be effected on the date of posting of the notice.
- The ATO has issued an impact statement where it confirms that it will treat the notices as served on the day of posting. This will reduce the time in which the recipient has to respond once the notice is received (if in fact it is received at all).

## Re: LED Builders Pty Ltd [2008] NSWSC 633

- An administrator of three companies in the Beechwood Group applied for an extension of the convening period of the second meeting of creditors. When the application was first listed for hearing, there was no evidence of the opinion of members of the committees of creditors of the companies on the merits of the application for extension.
- His Honour Justice Austin held that where there is a large amount owing to creditors, and there are many creditors as well as a committee of creditors, the Court will be assisted in considering the application by hearing the views of the members of the committee. Following an adjournment, the Court was advised that the committees generally supported the application and the orders for extension were made.

## Corporations Amendment Regulations (No 1) 2008

- These Regulations make minor amendments to the Corporations Regulations 2001 regarding the registered schemes annual review process for managed investment schemes.
- The amendments commenced on 4 June 2008.

## Cross Border Insolvency Act 2008

- This Act was assented to on 26 May 2008. Parts 2,3 and 4 (the operative provisions of the Act) commenced on 1 July 2008 as did the accompanying Regulations (Cross-Border Insolvency Regulations 2008). The Act gives effect to the Model Law on Cross Border Insolvency of the United Nations Commission on International Trade Law.
- The Act is intended to provide better mechanisms for dealing with cases of insolvency where the debtor's assets and creditors are located in multiple jurisdictions.

## News from Kemp Strang

- Peter Harrison has been elected a member of the NSW State Committee of the Insolvency Practitioners Association.
- Scott Hedge and Alex Linden have recently been named as two of Australia's leading lawyers in the area of insolvency and reorganisation inaugural edition of Best Lawyers Australia.

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