

The Proposed Deterrence of Phoenix Activity: An Opportunity Lost?

Helen Anderson*

Abstract

In late 2011, the Federal Government released draft legislation designed to tackle the abuse of the corporate form through phoenix activity, where a new company arises from the ashes of its failed predecessor. One of the laws has already been enacted while the other is not listed for debate in the current Parliament. While these are a step in the right direction, the former gives the Australian Securities and Investments Commission power to order the liquidation of dormant companies, and the other only deals with successor companies with similar names. These measures fail to confront the wider issues of improper phoenix activity, and are easily sidestepped. This article makes the case that the efficacy of present laws first needs to be assessed to determine whether the actual problem is a lack of enforcement. If it is accepted that new laws are needed to tackle phoenix activity properly, the government should look at successful international provisions which, for example, reverse the onus of proof on the qualification of directors of failed companies, or pierce the corporate veil on parent companies which have acted inequitably in relation to the creditors of their subsidiaries.

I Introduction

On 20 December 2011, the federal government released two exposure drafts of legislation designed to tackle phoenix company behaviour — the Corporations Amendment (Phoenixing and Other Measures) Bill 2012¹ and the Corporations Amendment (Similar Names) Bill 2012². The Bills were part of the Government's fulfilment of a 2010 pre-election commitment.³ On 22 March 2012 the Senate referred the Phoenixing Bill to the Economics Legislation Committee for inquiry and report.⁴ Its report was released on 9 May 2012, and

* Melbourne Law School, The University of Melbourne; Senior Research Fellow, Department of Business Law and Taxation, Monash University. The author thanks the Australian Research Council for its generous support for this research through its grant of \$144,000 over three years (DP1092474, 'Reform of the Personal Liability of Directors for Unpaid Employee Entitlements', 2010–12).

¹ Exposure Draft, Corporations Amendment (Phoenixing and Other Measures Bill) 2012 (Cth) ('Phoenixing Bill').

² Exposure Draft, Corporations Amendment (Similar Names) Bill 2012 (Cth) ('Similar Names Bill').

³ Julia Gillard and Labor, *Protecting Workers' Entitlements Package* Australian Labor Party <<http://www.alp.org.au/protecting-workers-entitlements-package/>>.

⁴ The Bill had already passed the House of Representatives Standing Committee on Economics, which found that 'the bill comprises uncontroversial measures that will assist in curbing the amoral

the Phoenixing Bill passed through the Senate, amid complaints from the opposition, that same day.⁵ This article argues that while the government's measures send a useful and timely message that phoenix activity is unacceptable, they fall far short of what is required to combat the behaviour effectively.

The concept of phoenix activity is notoriously difficult to define, but broadly centres on the idea of a new company arising from the ashes of its failed predecessor. There can be legitimate and beneficial reasons to start a similar business when an earlier entity fails, but frequently the behaviour involves the exploitation of the corporate form to the detriment of creditors. In one version of phoenix activity, a company in financial difficulties, 'Oldco', is placed into liquidation, voluntary administration ('VA') or is simply deregistered. Meanwhile, a new company, 'Newco', is incorporated and has the assets of Oldco transferred to it for inadequate consideration. Another version of phoenix activity involves arrangements within corporate groups where a subsidiary with few assets is liquidated without payment of its debts and an existing or newly created subsidiary takes over the activities of its failed sibling company. The term 'phoenix activity' is pejorative and therefore focuses on those resurrections where the corporate form has been abused and creditors have been duped out of the distribution they might otherwise have expected from the company's assets. A recent prominent example is *Australian Securities and Investment Commission v Somerville*,⁶ discussed below, where eight company directors were prosecuted for engaging in phoenix activity. For the first time, the Australian Securities and Investment Commission ('ASIC') also took action against the solicitor who facilitated the phoenix activity and was therefore held to be involved in the directors' breach of duties.⁷

The creditors hurt by phoenix activity include unsecured trade creditors, employees and revenue authorities. Employees may lose their accrued annual and long service leave entitlements, in addition to wages, redundancy and pay in lieu of notice. State and federal taxation authorities lose payroll tax revenue, and pay-as-you-go ('PAYG') instalments and superannuation amounts, deducted from employees' wages, are not remitted. In each case, there can be severe economic repercussions. Trade creditors may experience their own financial crises as a result. Employees are forced to rely on a taxpayer-funded safety net scheme which may not cover all their losses. The government suffers loss and the taxpayer is further burdened where properly levied taxation liabilities are unable to be recovered.

practice of phoenixing.' Commonwealth, *Parliamentary Debates*, House of Representatives, 27 February 2012, 1733 (Julie Owens).

⁵ Commonwealth, *Parliamentary Debates*, Senate, 9 May 2012, 2884–7 (Senator Cormann). The Senate Economics Legislation Committee's report was broadly supportive of the Bill, with recommendations for only minor amendments: Senate Economics Legislation Committee, Parliament of Australia, *Corporations Amendment (Phoenixing and Other Measures) Bill 2012* (2012). The report also contained a Coalition Senators' Dissenting Report: at 23–7.

⁶ (2009) 77 NSWLR 110 ('*Somerville*').

⁷ *Ibid* 126–7 [48]–[49].

A 2009 report showed that losses caused by phoenix activity have been mounting in Australia.⁸ The government's attention has now been attracted, possibly because losses to taxation authorities are estimated to run into the hundreds of millions of dollars.⁹ A press release in 2011, accompanying draft legislation to penalise the non-remittance of superannuation contributions,¹⁰ estimated that there were 6000 phoenix companies in Australia.¹¹ Since 2009, the government has introduced a series of small measures to attempt to address phoenix activity. For example, in 2010, some minor changes were enacted to improve the rights of the ATO to require security bonds in relation to expected future tax debts. In late 2011, the two further Bills that are the subject of this article were released for public comment. Bravely heralded as '[stopping] directors from exploiting the limited liability protections in the corporations law',¹² in reality the proposed legislation does little to help those adversely affected by fraudulent phoenix activity and even less to deter company controllers from this harmful behaviour.

This article argues that the time is ripe for an extensive and careful overhaul of the relevant law and its enforcement mechanisms. It begins in Part II with the background to phoenix activity and the response it has received in Australia. Part III looks at taxation legislation which has been enacted or proposed in response to the Government's concern over revenue loss as a result of phoenix activity. Part IV considers the current corporate law environment to see what gaps the 2011 Bills are purporting to fill. Part V examines the *Corporations Amendment (Phoenixing and Other Measures) Act 2012* (Cth) ('*Phoenixing Act*') and the Similar Names Bill. Part VI brings these discussions together to ask whether these instruments will achieve what was promised by the Government, or whether the Government needs to look further afield for inspiration. Part VII concludes.

II The Recognition of Phoenix Activity in Australia

The earliest report dealing exclusively with improper phoenix activity was that of the Victorian Parliament Law Reform Committee ('VPLRC') in 1994.¹³ The main recommendations — all sensible and practical — were to tighten the laws governing the disqualification of directors of companies, allocate more resources to detection and prosecution of offenders, change public and judicial attitudes to acknowledge the seriousness of this type of white-collar crime, improve information flows between regulators, and enact laws to allow the freezing of

⁸ Treasury (Cth), 'Action against Fraudulent Phoenix Activity' (Proposals Paper, Treasury, Australian Government, November, 2009) 5–6 ('*2009 Phoenix Proposals Paper*').

⁹ *Ibid* 5.

¹⁰ This is discussed further below. The superannuation guarantee charge is administered by the Australian Taxation Office ('ATO').

¹¹ Bill Shorten, 'Protecting Employee Super and Strengthening the Obligations of Company Directors' (Media Release, No 138, 13 October 2011).

¹² David Bradbury, 'Gillard Government Releases Draft Laws to Crack Down on 'Phoenixing'' (Media Release, No 66, 20 December 2011).

¹³ Law Reform Committee, Parliament of Victoria *Curbing the Phoenix Company: First Report on the Law Relating to Directors and Managers of Insolvent Corporations* (1994) ('*1994 VPLRC Report*').

assets over which a company has a claim.¹⁴ In response, in 1998 the ATO instituted the ‘Phoenix Project’, which allocated more staff to work with other agencies to address the phoenix problem.¹⁵ In 1999, the director disqualification provisions were consolidated but not significantly tightened.¹⁶ The *1994 VPLRC Report* also recommended legislation to restrict the use of business names similar to those of the failed corporation, based on legislation in the United Kingdom.¹⁷ This final recommendation is the somewhat belated subject of one of the pieces of proposed legislation dealt with in this article.

In 2003, the Royal Commission into the Building and Construction Industry (‘*Cole Royal Commission*’) produced a lengthy report containing many recommendations, including a chapter devoted to phoenix companies.¹⁸ Among its many adverse consequences, Commissioner Cole noted that phoenix behaviour even affects competitors. Companies that fail to pay taxes, superannuation contributions and employee entitlements can undercut prices in tenders made by law-abiding companies,¹⁹ which may be induced to act in a similar manner if phoenix activity is not detected and prosecuted. Its recommendations included increasing liaison and information flows between Commonwealth and state revenue authorities²⁰ and between the ATO and ASIC;²¹ and changing the law to allow the disqualification of directors after being associated with one failed company.²² The latter recommendation was not adopted, but the period of potential disqualification for directors was doubled in 2004.²³ The *Cole Royal Commission* also recommended corporate group liability in relation to certain tax debts of other group members.²⁴ This was not adopted.

¹⁴ Ibid 19 [3.1.26], [3.1.28], 23–4 [3.2.21]–[3.2.22], 27 [3.3.12], 40–1 [4.1.44]. The recommendations were changed slightly after a consideration of disqualification procedures internationally (dealt with in Law Reform Committee, Parliament of Victoria, *Curbing the Phoenix Company: Second Report* (1994)) and the final recommendations were then summarised in Law Reform Committee, Parliament of Victoria, *Curbing the Phoenix Company: Third Report on the Law Relating to Directors and Managers of Insolvent Corporations* (1995).

¹⁵ These efforts were outlined in ATO, Submission to Royal Commissioner, *Royal Commission into the Building and Construction Industry*, June 2002, 8 [37], 10–11 [55]–[63].

¹⁶ The director disqualification provisions were amended by the *Corporate Law Economic Reform Program Act 1999* (Cth). The various grounds for disqualification were brought together in one place: *Corporations Law* (Cth) pt 2D.6, now *Corporations Act 2001* (Cth) pt 2D.6. The wording changed slightly from the former provisions but it did not substantially change the law.

¹⁷ *1994 VPLRC Report*, above n 13, 54 [4.4.18]. The United Kingdom provisions referred to were *Insolvency Act 1986* (UK) c 45, ss 216–17.

¹⁸ Commonwealth, *Royal Commission into the Building and Construction Industry, Final Report* (2003) vol 8 ch 12 (‘*Cole Royal Commission Final Report*’).

¹⁹ Ibid 119 [26], 133–4 [93]–[98].

²⁰ Ibid vol 1, 107, recommendation 102.

²¹ Ibid vol 1, 109, recommendation 105.

²² Ibid vol 1, 111, recommendation 109.

²³ The period of the disqualification is up to 20 years, increased from 10 years by the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (Cth), as a result of recommendations from the Cole Royal Commission: Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Corporate Insolvency Laws: A Stocktake* (2004) 142 [8.47] (‘*2004 Stocktake Report*’).

²⁴ *Cole Royal Commission Final Report*, above n 18, 106, recommendation 101. To achieve this, the Commission recommended that states and territories adopt the *Pay-Roll Tax Act 1971* (NSW) s 16LA.

Shortly after the *Cole Royal Commission*, the *2004 Stocktake Report*²⁵ looked at a broad range of issues, including phoenix activity.²⁶ It, too, produced a series of recommendations designed to increase its detection and prosecution. Echoing the *Cole Royal Commission Final Report*, the *2004 Stocktake Report* recommended that disqualification be available where a director was associated with a single failed company.²⁷ It also called for the release of the government's response to the Companies and Securities Advisory Committee's 2000 *Corporate Groups: Final Report*,²⁸ which had canvassed a wide range of measures for piercing the corporate veil on corporate groups.²⁹ Other recommendations related to administrative improvements to databases and the establishment of a hotline for the reporting of phoenix activity.³⁰ As the *1994 VPLRC Report* had done a decade before, the *2004 Stocktake Report* called for the freezing of assets over which creditors have a just claim, without specifying the basis of such a claim.³¹ This was not acted upon.

Despite the increasing clamour regarding the deleterious effects of phoenix activity, little was done to implement the measures suggested by this series of reports. In 2009, the Australian Government Treasury released a proposals paper entitled 'Action Against Fraudulent Phoenix Activity'.³² It canvassed options to address 'fraudulent phoenix activity', which is estimated to cost the ATO AU\$600 million per year.³³ Its costs to other creditors were not estimated in the report but were considered 'significant'.³⁴ The *2009 Phoenix Proposals Paper* described a newly-incorporated company taking over the business of a previously liquidated entity which has failed to pay its debts as the 'basic' form of phoenixing,³⁵ and phoenix activity within corporate groups as the 'sophisticated' form.³⁶ Typically, under the sophisticated form, one entity with few assets within a corporate group incurs substantial liabilities by way of wages, superannuation contributions, PAYG or sales tax, and then is liquidated. If they are 'lucky', the employees may be transferred to another entity in the group to continue their employment, without necessarily being paid their entitlements. Taxation authorities, as non-priority unsecured creditors, are left empty handed. While the main focus of the report was on phoenix activity as it related to non-payment of taxation liabilities, it also made several recommendations for *Corporations Act* reform.³⁷ As the *1994 VPLRC*

²⁵ *2004 Stocktake Report*, above n 23, ch 8.

²⁶ Its terms of reference included '(h) whether special provision should be made regarding the use of phoenix companies': *ibid* vii.

²⁷ *2004 Stocktake Report*, above n 23, 144–5 [8.59], recommendation 31.

²⁸ Companies and Securities Advisory Committee, Parliament of Australia, *Corporate Groups: Final Report* (2000).

²⁹ *2004 Stocktake Report*, above n 23, 144–5 [8.59], recommendation 36.

³⁰ *Ibid* 147[8.69], 150 [8.84], [8.86], recommendations 32, 34 and 35.

³¹ *Ibid* 149 [8.89], recommendation 33.

³² *2009 Phoenix Proposals Paper*, above n 8, [1.1].

³³ *Ibid* 5.

³⁴ *Ibid*.

³⁵ *Ibid* 2.

³⁶ *Ibid*.

³⁷ These recommendations were to allow the corporate veil to be lifted where a company sets up a subsidiary with insufficient capital to meet the debts that could reasonably be expected to arise, and to make directors personally liable for the debts of a liquidated company in circumstances where a 'new' company adopts the same or a similar name as its previous incarnation: *ibid* 19–21.

Report had done, it recommended laws imposing liability on directors where they started up a new company with a similar name to the previous defunct one.

The *2009 Phoenix Proposals Paper* indicated that ‘the existing mechanisms provide little incentive not to phoenix, and remedial action is conducted on a case by case basis, well after the damage has been done.’³⁸ It noted that the director penalty notice (‘DPN’) provisions, which impose personal liability on directors for unremitted withholding taxes unless the company is promptly placed into external administration, did not cover unpaid superannuation guarantee charge amounts.³⁹ The non-reporting and non-payment of these withholding taxes do not become apparent until the end of the financial year, by which time liabilities have reached a significant amount. This defeats one of the purposes of the DPN regime,⁴⁰ which is to provide a strong incentive for directors to act swiftly to ensure companies prevent liabilities escalating. Another problem identified by the *2009 Phoenix Proposals Paper* was the resource-intensive nature of the imposition of a DPN by the ATO, which meant that many directors escaped liability.⁴¹ As a result, the paper suggested that the DPN regime be automated, subject to a change in time limits.⁴² In addition, it proposed that the legislation should remove the ability of directors engaged in fraudulent phoenix activity to avoid personal liability for withholding liabilities by placing the company into VA or liquidating the company.⁴³

III Taxation Legislation to Tackle Phoenix Activity

In response to the *2009 Phoenix Proposals Paper*, some relevant tax laws were changed in 2010, although they were scarcely ground-breaking reforms. None of the principal options from the *2009 Phoenix Proposals Paper* were included in the new legislation. Instead, the director penalty notice provisions were moved⁴⁴ and amended in a minor way. Section 269-15 of the *TAA* sets out the directors’ obligation to ‘cause the company to comply with its obligation’ to pay its tax liability, which continues until the company has paid that tax or is wound up or placed in voluntary administration. As with the previous legislation, directors become liable for a penalty if they do not cause the company to pay its liabilities by the due date. There are two noteworthy differences from the previous legislation.⁴⁵ First, a director has 21 days to meet the requirements of the notice,

³⁸ *Ibid* 7.

³⁹ *Ibid* 9

⁴⁰ This was introduced in 1993 by the *Insolvency (Tax Priorities) Legislation Amendment Act 1993* (Cth).

⁴¹ *2009 Phoenix Proposals Paper*, above n 8.

⁴² *Ibid* 13.

⁴³ *Ibid* 13–14. Other tax recommendations included ensuring that there are anti-avoidance provisions in the taxation law (either through an expansion of the existing general anti-avoidance rule (‘GAAR’) or through the creation of a specific provision) to effectively negate any taxation benefit derived from fraudulent phoenix activity: at 15–16.

⁴⁴ The *Tax Laws Amendment (Transfer of Provisions) Act 2010* (Cth) moved the DPN provisions from the *Income Tax Assessment Act 1936* (Cth) to the *Taxation Administration Act 1953* (Cth) sch 1 (‘TAA’).

⁴⁵ There are a number of other changes, including the clarification as to the date when notice is given: *TAA* sch 1 s 269-25(4). The illness defence has also been clarified and tightened: s 269-35(2). The law also confirmed that the Court has no power under s 1318 of the *Corporations Act* to grant relief

rather than 14 days.⁴⁶ Second, if the company enters into a repayment agreement with the Commissioner, a director's obligation to cause the company to comply with its obligation, and subsequent penalty for failure to do so, is not removed or remitted. Rather, that obligation remains and the Commissioner is simply unable to collect the money or penalty while an instalment agreement is in place.⁴⁷ Under the previous provision, entering into the instalment agreement removed the director's penalty and a new one had to be created if the agreement failed. The amendment simplifies the collection mechanism.

As noted in the introduction, the new laws also enable the Commissioner to obtain security from a taxpayer for any existing or future tax liability, including the superannuation guarantee charge, if the Commissioner considers that the taxpayer intends to carry on an enterprise for a limited time only, or if it is otherwise appropriate.⁴⁸ Failure to pay the security is an offence, punishable by a fine.⁴⁹ The ATO's 'Annual Report 2010–11' noted that the ATO finalised 133 phoenix cases and raised AU\$70.7 million in taxes and penalties. In addition, the ATO issued 10 security bond demands to phoenix operators relating to an existing or future debt.⁵⁰

At first glance, one wonders why these essentially procedural amendments were needed. In the tax realm, the *Crimes (Taxation Offences) Act 1980* (Cth) already imposes criminal sanctions where a person enters into an arrangement with the intention of securing that a company will be unable to pay income tax or a range of other taxes including the superannuation guarantee charge.⁵¹ Aiding and abetting such an arrangement or transaction by another is also covered.⁵² The penalties are 10 years imprisonment or 1000 penalty units or both. The existence of these penalties is publicised by the ATO via its taxpayer alerts.⁵³ However, it is possible that this criminal offence, involving as it does the requirement to prove the accused's intention beyond reasonable doubt, is simply too difficult to establish. As will be seen below, a similar argument has been made with respect to legislation designed to penalise transactions to defeat the payment of employee entitlements.

On 5 July 2011, the Treasury released for public consultation an exposure draft of 'tax law amendments to strengthen company director obligations and deter

to a director from their obligations in respect of a director penalty, confirming the rule in *Deputy Commissioner of Taxation v Dick* (2007) 242 ALR 152, 164 [78] (Santow JA) (New South Wales Court of Appeal).

⁴⁶ TAA sch 1, s 269-25(1).

⁴⁷ Ibid, s 269-15(3).

⁴⁸ Ibid sub-div 255-D. Previously, the Commissioner could only ask for a security bond or deposit for income tax liabilities: *Income Tax Assessment Act 1936* (Cth) s 213. There is also a broadening of its reach in that the old law covered a 'business', and the new law covers 'enterprises'.

⁴⁹ TAA sch 1, s 255-110.

⁵⁰ ATO, 'Annual Report 2010–11', (Abbyak Report, ATO, 30 September 2011) 102.

⁵¹ *Crimes (Taxation Offences) Act 1980* (Cth) ss 5 and 17. Note that there are also penalties which can be imposed under the *Criminal Code* (Cth) for defrauding a Commonwealth entity (s 135.1) or for conspiracy to defraud a Commonwealth entity (s 135.4).

⁵² *Crimes (Taxation Offences) Act 1980* (Cth) ss 6 and 7.

⁵³ See, eg, ATO, Taxpayer Alert: *Liquidation of Entities to Avoid the Payment of Tax Liability*, No 16 of 2008, 25 June 2008.

fraudulent phoenix activity'.⁵⁴ The release of the two Bills — the Tax Laws Amendment (2011 Measures No 8) Bill 2011 (Cth) and the Pay As You Go Withholding Non-compliance Tax Bill 2011 (Cth) — acknowledged that '[w]hile these amendments aim to deter fraudulent phoenix activity, they apply more broadly to extend the personal obligations of company directors to ensure that the company complies with its PAYG withholding and superannuation guarantee obligations.'⁵⁵ Under the amendments, the ATO would be allowed to pursue directors immediately under the director penalty regime if the company's unpaid PAYG withholding and superannuation guarantee liabilities remained unpaid and unreported three months after becoming due, without the need to issue a penalty notice. This was intended to relieve some of the enforcement burden felt by the ATO.

However, on the recommendation of the House of Representatives Standing Committee on Economics, which was responding to fears raised by the business lobby, these amendments were not passed by Parliament in late 2011.⁵⁶ Revised drafts of these Bills⁵⁷ were released for public comment in April 2012 and passed through the Parliament, following a favourable report by the House of Representatives Standing Committee on Economics at the end of June 2012.⁵⁸ The new laws are still unpopular with business because they lack an accepted definition of phoenix activity, and, accordingly, directors acting in good faith and attempting to comply with their obligations could also be penalised. Unfortunately, the *Tax Laws Amendment (2012 Measures No 2) Act 2012* (Cth) has removed the proposed automated director penalty notice, which was a feature of the 2011 Bill, which means that the onus is back on the ATO to detect breaches and enforce the law.

IV Current Corporations Legislation Relevant to Phoenix Activity

After nearly two decades of reports and relatively little action, it appears that the government's response to phoenix activity has been confined to tinkering at a micro level with taxation laws, and that even some of those reforms are being stymied by the vigorous objections of business representatives. Before considering the amendments to the *Corporations Act* proposed by the government at the end of 2011, it is instructive to look at the current provisions of the Act under which phoenix activity could be addressed. There is no specific section which defines phoenix activity or makes it illegal, and the term is not found within the *Corporations Act*.

⁵⁴ Treasury (Cth), 'Exposure Draft — Tax Law Amendments to Strengthen Company Director Obligations and Deter Fraudulent Phoenix Activity' (Press Release, No 2073, 5 July 2011).

⁵⁵ *Ibid.*

⁵⁶ House of Representatives Standing Committee on Economics, Parliament of Australia, *Advisory Report on the Tax Laws Amendment (2011 Measures No 8) Bill and the Pay As You Go Withholding Non-compliance Tax Bill 2011* (2011) 35–6 [2.78]–[2.80].

⁵⁷ Tax Laws Amendment (2012 Measures No 2) Bill 2012 (Cth); Pay As You Go Withholding Non-compliance Tax Bill 2012 (Cth) ('PAYG Non-compliance Bill').

⁵⁸ House of Representatives Standing Committee on Economics, Parliament of Australia, *Advisory Report on the — Tax Laws Amendment (2012 Measures No 2) Bill 2012, Pay As You Go Withholding Non-compliance Tax Bill 2012, Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, Passenger Movement Charge Amendment Bill 2012* (2012).

The fact remains that substantial penalties already exist for engaging in phoenix activity, as it is generally understood. Directors may be disqualified, ordered to pay a pecuniary penalty or to pay compensation. Companies may be wound up where it is just and equitable. It raises the question whether it is a paucity of law, or a lack of detection and enforcement, which allows phoenix activity to survive. If the latter, then measures have to be taken to improve detection and enforcement, such as government allocation of extra resources to regulators, combined with clear signals that stamping out this behaviour is a priority. To complement these endeavours, any law reform needs to be framed in such a way that it simplifies both detection and enforcement. Suggestions to this effect are discussed below in Part VI E.

A Disqualification

It is important to stress that it is not unlawful to be involved in the management of an unsuccessful business or a succession of unsuccessful businesses. It is to be expected that a person who fails in one enterprise will attempt to start another business, and if their skills and knowledge are in a particular area, the new business is likely to be in that same area. Lessons should have been learned. It is possible that the earlier failure was caused by conditions extrinsic to the company and does not reflect on the business acumen of its owners.

As a result, there is no automatic disqualification of directors for being an officer of a failed business, although the Court has a discretion to disqualify where the director has been involved in two or more failed companies in seven years, and 'it is satisfied that ... the manner in which the corporation was managed was wholly or partly responsible for the corporation failing, ... and the disqualification is justified'.⁵⁹ ASIC itself may disqualify a director where an adverse liquidator's report has been lodged for each of the two failed companies.⁶⁰ While these provisions are useful, they cannot be used in the first resurrection of the failed company. There are further powers to disqualify for repeated contraventions of the Act⁶¹ and civil penalty breaches.⁶² ASIC is required to keep a register of disqualified persons,⁶³ and this may be searched online by the public without charge.⁶⁴

⁵⁹ *Corporations Act* s 206D(1)(b).

⁶⁰ *Ibid* s 206F. This is a report under s 533, which relates to the misapplication of company assets, breaches of duty, or the fact that the company may be unable to pay its creditors more than 50 cents in the dollar. Clearly ASIC's power to disqualify under this section is contingent on the company being in liquidation rather than VA or simply deregistered by ASIC.

⁶¹ *Ibid* s 206E.

⁶² *Ibid* s 206C. See above n 16 and accompanying text.

⁶³ *Ibid* s 1274AA.

⁶⁴ ASIC, *Professional Registers* (29 March 2012) <<http://www.asic.gov.au/asic/asic.nsf/byheadline/Professional+registers?openDocument>>.

B *Directors' Duties*

The directors' duties powers contained in ss 180–184 of the *Corporations Act* can be used by ASIC or the company's liquidator against company directors who misuse their powers by engaging in phoenix activity. Under s 181(1), directors must exercise their powers in good faith in the best interests of the company and for a proper purpose. Under s 182(1), directors must not improperly use their position: to gain an advantage for themselves or someone else, or to cause detriment to the corporation. Many of the actions of directors who engage in phoenix activity would amount to breaches of these duties, which have criminal equivalents under s 184 or may be actioned by ASIC as civil penalty breaches under pt 9.4B of the *Corporations Act*.

An early example is *Jeffree v National Companies and Securities Commission*.⁶⁵ There, the director of a company that faced an adverse commercial arbitration decision transferred the company's business name and assets to another company. The consideration paid to the company for the transfer was sufficient to meet trade creditor claims but left nothing to satisfy the arbitration award. This was held to be an improper use of information acquired in his position as a director, contrary to the equivalent of the *Corporations Act* s 183. Another example is *R v Heilbronn*,⁶⁶ where the director of a company with substantial sales tax liabilities stripped the company of its assets and transferred them to another company, and then to a third company. On each occasion, the same business was carried under the same trading name. A proper price was not paid for the assets and no effort was made to ensure that liabilities and legal obligations under the *Corporations Act* had been met. The director, Heilbronn, was found to have knowingly and intentionally defrauded the creditors of the second company and, in doing so, made an improper use of his position as officer to cause detriment to that company.⁶⁷ He was sentenced to two years imprisonment.

Somerville is a recent case⁶⁸ where the New South Wales Supreme Court found eight directors to have acted in breach of ss 181(1), 182(1) and 183(1) of the *Corporations Act* by engaging in illegal phoenix activity. Their solicitor, Timothy Somerville, also contravened s 79 of the *Corporations Act* as a person involved in the contravention of the Act, as he aided and abetted the directors in their breaches. In each of the cases, assets were transferred from the financially distressed companies to new companies, in consideration of the issue of V class shares which supposedly carried an entitlement to a dividend from the new company. Windeyer J found that there was 'no proper basis for the transactions other than to keep the benefit of the assets in [the new] company without the burden of liabilities'.⁶⁹

⁶⁵ [1990] WAR 183.

⁶⁶ (1999) 150 FLR 43.

⁶⁷ This was a breach of s 232(6) of the *Corporations Law* (Cth), as it then was (now *Corporations Act*) s 182). It was therefore a civil penalty breach. Because of Heilbronn's intentionally dishonest behaviour, it became a criminal offence under the equivalent of the present s 184(2).

⁶⁸ (2009) 77 NSWLR 110.

⁶⁹ *Ibid* 125 [42].

Importantly, ASIC's right to take action does not depend on the company's status as a going concern or on the form of its external administration. There is also a range of orders which the court can make on ASIC's application: pecuniary penalties,⁷⁰ compensation⁷¹ and disqualification of the director.⁷² In addition, directors breaching their duties recklessly or with intentional dishonesty may be subject to criminal proceedings and penalties of up to AU\$220 000, five years imprisonment or both.⁷³ These are heavy consequences and should therefore be a powerful deterrent against phoenix activity. It should also be noted here that even under general law fiduciary duties, courts have allowed claims for equitable remedies against directors who have misused their position to benefit their new company at the expense of the old one.⁷⁴

C *Winding Up on the Just and Equitable Ground*

Corporations legislation in Australia has long provided for the winding up of companies on the just and equitable ground.⁷⁵ It may be ordered by the court on the application of ASIC, a shareholder or a creditor.⁷⁶ For example, in *ASC v AS Nominees Ltd*,⁷⁷ ASIC's predecessor successfully sought the winding up of a company where its directors had acted in breach of their fiduciary duties to avoid a conflict of interest. Likewise, the Deputy Commissioner of Taxation, as a contingent creditor in *Deputy Commissioner of Taxation v Casualife Furniture International Pty Ltd*,⁷⁸ had the standing to seek the winding up of a company with a 20-year history of phoenix activity leaving unpaid taxes. Hansen J found the winding up to be in the public interest and conducive to commercial morality. He said:

The facts and circumstances set out in this judgment describe an unhappy approach to corporate, directorial or management responsibility. ... [a]s one entity has collapsed, and been wound up with a debt to the Commissioner of Taxation (and others), it has been found that the assets have been shifted to another entity which is found to be conducting the business, and the pattern repeats itself. ... [a]ll of this has been, and remains, a structure deliberately created by Joseph Guss for the purpose of ensuring the ongoing control of the business by the Guss family, come what may.⁷⁹

⁷⁰ *Corporations Act* s 1317G.

⁷¹ *Ibid* s 1317H.

⁷² *Ibid* s 206C.

⁷³ *Ibid* s 184, sch 3 item 30.

⁷⁴ See, eg, *Ferrari Investment (Townsville) Pty Ltd (in liq) v Ferrari* [2000] 2 Qd R 359, 372–3 [47].

⁷⁵ *Corporations Act* s 461(1)(k).

⁷⁶ *Ibid* s 462.

⁷⁷ (1995) 62 FCR 504.

⁷⁸ (2004) 9 VR 549 ('*Casualife*'). See also *Deputy Commissioner of Taxation v Woodings* (1994) 13 WAR 189 ('*Woodings*'), discussed below in Part VI C.

⁷⁹ *Casualife* (2004) 9 VR 549, 580 [494]–[495].

D *Transactions to Deprive Employees of Their Entitlements*

The appointment of a liquidator allows action to be taken under *Corporations Act* s 596AB against directors entering into transactions with the intention of preventing the recovery of the entitlements of employees of a company, or significantly reducing the amount of the entitlements of employees of a company that can be recovered. According to the Explanatory Memorandum which preceded the enactment of the *Corporations Law Amendment (Employee Entitlements) Act 2000* (Cth), the object of s 596AB was ‘to deter the misuse of company structures and of other schemes to avoid the payment of amounts to employees that they are entitled to prove for on liquidation of their employer’.⁸⁰

Yet the section has never been effectively used. This should come as no surprise. The legislation had its second reading speech on 17 February 2000. When debate resumed on 9 March, the Labor opposition quickly expressed its disappointment with the legislation, and the difficulty with having to prove an intention to deprive employees of their entitlements was pointed out.⁸¹ The Bill was referred to the Parliamentary Joint Statutory Committee on Corporations and Securities.⁸² Numerous objections were made.⁸³ One submission noted that the provisions would be a ‘toothless tiger’ that would be ‘so hard to prove that nobody will be effectively prosecuted.’⁸⁴ As predicted, the legislation enacted in 2000 proved ineffective. The *2004 Stocktake Report* recommended that it be reviewed and:

[i]n light of the evidence suggesting that some corporations deliberately structure their business to avoid paying their full entitlements to employees and more generally unsecured creditors, the Committee recommends that the review look beyond the effectiveness of the Act and consider, and offer advice on, possible reforms that would deter this type of behaviour.⁸⁵

This recommendation was not acted upon. The Joint Committee of Public Accounts and Audit in 2008 noted an increase in the numbers of individuals

⁸⁰ Explanatory Memorandum, *Corporations Law Amendment (Employee Entitlements) Bill 2000* (Cth) 5 [18]. Section 588G was also amended to allow uncommercial transactions under s 588FB to be pursued as insolvent trading. The Explanatory Memorandum acknowledged that ‘The inclusion of uncommercial transactions in section 588G(1A) has implications for the protection of employee entitlements, the prosecution of directors involved in “phoenix” activity and recovery actions by liquidators for the benefit of creditors generally’: at 4 [10].

⁸¹ Commonwealth, *Parliamentary Debates*, House of Representatives, 9 March 2000, 14301–4 (Kelvin Thomson); Commonwealth, *Parliamentary Debates*, House of Representatives, 15 March 2000, 14806 (Dick Adams).

⁸² Commonwealth, *Official Committee Hansard*, Joint Committee on Corporations and Securities, ‘Reference: Corporations Law Amendment (Employee Entitlements) Bill 2000’, 5 April 2000.

⁸³ Parliamentary Joint Statutory Committee on Corporations and Securities, *Parliament of Australia Report on the Corporations Law Amendment (Employee Entitlements) Bill 2000*, (2000) 7–16.

⁸⁴ Submission by the Shop, Distributive and Allied Employees’ Association: *ibid* 11 [3.25]. The Australian Council of Trade Unions also opposed the intention requirement, arguing that it was ‘an impossible burden that significantly reduced the effect of the section’ at 10 [3.21]. A similar view was taken by the Textile, Clothing and Footwear Union of Australia (Victorian Branch) and the Australian Catholic Commission for Industrial Relations: at 11 [3.27] and [3.28].

⁸⁵ *2004 Stocktake Report*, above n 23, 185 [10.67] recommendation 43.

promoting the benefits of fraudulent phoenix activity,⁸⁶ and at its hearings, ATO Deputy Commissioner Mark Konza expressed his frustration that the fight against phoenix activity was being thwarted by light penalties and a lack of prosecutions.⁸⁷ The *2009 Phoenix Proposals Paper* acknowledged that '[i]t is clear that ... existing mechanisms do not provide a sufficient disincentive to prevent fraudulent phoenix activity.'⁸⁸ This is undoubtedly true. In *Fair Work Ombudsman v Ramsey Food Processing Pty Ltd* in the Federal Court in October 2011, Buchanan J spoke of the 'interpositioning' of an assetless company between employees and their true employer, 'for the purpose of avoiding direct legal responsibility for the wages and entitlements of employees. ... A purpose of that kind does not mean, necessarily, that arrangements are ineffective, much less illegal.'⁸⁹

V The *Phoenixing Act* and the Similar Names Bill

Against this background, just prior to Christmas 2011, the federal government released two exposure drafts of legislation — the Corporations Amendment (Phoenixing and Other Measures Bill) 2012, passed into legislation in May 2012 (*Phoenixing Act*) and the Corporations Amendment (Similar Names) Bill 2012. These recognise that phoenix activity affects more than taxation authorities, and takes up one of the recommendations of the *2009 Phoenix Proposals Paper* in relation to the resurrection of a company with a similar name to that of its liquidated predecessor. Upon the release of the two Bills, the Parliamentary Secretary to the Treasurer, the Hon David Bradbury, made the following claims:

These amendments will crack down on 'phoenixing', where directors try and avoid having to pay workers' entitlements and other unsecured creditors by restarting their failed business using a similar company name, sometimes located in the same premises with the same staff and clients.

Under these proposals, directors of a failed company can be held liable for the debts of a company that has a similar name to a pre-liquidation name of the failed company — otherwise known as a phoenix company.

This will stop directors from exploiting the limited liability protections in the corporations law to avoid having to pay any debts, including workers' entitlements, that they incur in a 'phoenix' company.

This will ensure that directors cannot keep racking up debts through multiple 'phoenix' companies and escape their obligations to pay workers' entitlements and other creditors.⁹⁰

These were very ambitious claims, and seemed to promise that the government had finally heeded the repeated calls for legislation to tackle phoenix activity. Yet both instruments are extremely limited in their scope. The *Phoenixing*

⁸⁶ Joint Committee of Public Accounts and Audit, Parliament of Australia, *Report 410: Tax Administration* (2008), 42, [2.48].

⁸⁷ Evidence to Joint Committee of Public Accounts and Audit, Parliament of Australia, Canberra, 23 October 2009, 24 (Mark Konza, Deputy Commissioner of Taxation).

⁸⁸ *2009 Phoenix Proposals Paper*, above n 8, 7.

⁸⁹ (2011) 198 FCR 174, 176–7 [2]–[3] (*Ramsey*).

⁹⁰ Bradbury, above n 12.

Act gives ASIC the power to order the winding up of a company where it becomes apparent that it is not carrying on business, evidenced for example by the non-return of ASIC forms or the non-payment of fees.⁹¹ ASIC may then appoint a liquidator to wind up the affairs of the company. This is intended to overcome the problem of companies which remain dormant with unpaid debts, and where no creditor seeks the appointment of a liquidator. The liquidator is meant to uncover breaches of the law, including phoenix activity, and bring appropriate action. In addition, the liquidation of the company will allow employees to have access to the General Employee Entitlements and Redundancy Scheme ('GEERS'), the taxpayer-funded safety net scheme for unpaid wages and other entitlements for employees of insolvent employers. This was one of the major advances which the Parliamentary Secretary trumpeted in announcing the proposed legislation.⁹² In addition, the *Phoenixing Act* allows for the publication of corporate insolvency notices through a single, publicly available website.⁹³

The second piece of proposed legislation, the Similar Names Bill, provides that a director of a failed company can be jointly and individually liable for the debts of a company that has a similar name to a pre-liquidation name of the failed company.⁹⁴ Certain time limits are specified.⁹⁵ This follows the example of several overseas jurisdictions, such as the United Kingdom⁹⁶ and New Zealand.⁹⁷ A similar name is sometimes used for the phoenix company so that customer goodwill can be maintained and cheques payable to the previous entity can be banked in the new company's bank account. According to the Bill, the court may make exemptions 'where the person has acted honestly ... and having regard to all the circumstances of the case, the person ought fairly to be exempt,'⁹⁸ with certain matters specified to which the court must have regard, including 'the extent to which, and the circumstances in which, any assets of the failed company have become assets of the debtor company'.⁹⁹ The failed company's liquidator is also empowered to make a similar determination.¹⁰⁰ An exemption is also granted if the failed company has paid its debts in full.¹⁰¹

VI Analysis of the *Phoenixing Act* and the Similar Names Bill

Despite the wide recognition of the damage caused by phoenix activity and the benefits that the new Act and the proposed Bill will bring, the Parliamentary

⁹¹ *Phoenixing Act* sch 1 item 1, inserting *Corporations Act* s 489EA.

⁹² Explanatory Memorandum, Corporations Amendment (Phoenixing and Other Measures) Bill 2012 (Cth) 5–6 [1.2]–[1.3]; see also Bradbury, above n 12.

⁹³ *Phoenixing Act* sch 1 pt 2. Draft regulations to provide for the establishment of an insolvency notices website to be managed by ASIC from 1 July 2012 were released for public comment on 17 May 2012: Exposure Draft, Corporations Legislation Amendment Regulations 2012 (Cth).

⁹⁴ Similar Names Bill sch 1 item 1, inserting *Corporations Act* s 596AJ(1).

⁹⁵ *Ibid* sch 1 item 1, inserting *Corporations Act* ss 596AJ(1)(b) and (d).

⁹⁶ *Insolvency Act 1986* (UK) c 45, s 216.

⁹⁷ *Companies Act 1993* (NZ) s 386A.

⁹⁸ Similar Names Bill sch 1 item 1, inserting *Corporations Act* s 596AK(3).

⁹⁹ *Ibid*, inserting *Corporations Act* s 596AK(4)(b).

¹⁰⁰ *Ibid*, inserting *Corporations Act* s 596AK(4)(b), s 596AL.

¹⁰¹ *Ibid*, inserting *Corporations Act* s 596AN.

Secretary's claims noted above are not justified. The amendments might make some slight inroads in the case of basic phoenixing but do nothing about sophisticated phoenixing in corporate groups. Apart from the improved access to GEERS that will flow from the *Phoenixing Act*, discussed below, nothing has been done or is proposed to be done to protect employee entitlements or the rights of other unsecured creditors. Nothing has been done with regard to phoenix activity within VAs. The government must therefore acknowledge that more is needed.

Passing comprehensive laws to deal with phoenix activity is an undeniably complex matter.

Fraudulent phoenix activity must be distinguished from a proper acquisition of an insolvent company's assets, often under a VA, which saves some or all of the business of the insolvent company. This could, for example, come through the perfectly legal buyout of the business, by management or some other company, or through the 'pre-pack'¹⁰² purchase of the assets immediately upon the appointment of the liquidator. In these circumstances there may be genuine benefits to all creditors if a good price is paid for these assets. If the business can continue under a new corporate entity, employment may continue without interruption, and most, if not all, liabilities can be discharged. Even if the subsequent business does not succeed, the attempt does not render the actions of the directors illegal or even necessarily improper. One of the opposition's main objections to the Phoenixing Bill was that it had the potential to affect all companies rather than those actually engaged in improper phoenix activity,¹⁰³ and for this reason it opposed its passage in the House of Representatives and the Senate.

Legislation to tackle phoenix activity therefore needs to be meticulously considered and integrated to ensure that it achieves a set of pre-defined, carefully articulated overall objectives. Because phoenix activity has the capacity to mimic quite legitimate and indeed, beneficial, behaviour, any laws to deter the illegitimate version must be balanced against any harm they may cause. This is also the case with the sophisticated form of phoenix activity within corporate groups. The corporate group is the dominant structure of business organisation for large enterprises, both in Australia and elsewhere in the world. In 1997, Ramsay and Stapledon found that 89 per cent of the top 500 companies listed on the Australian Stock Exchange had at least one controlled entity and on average, each listed company had 28 controlled entities.¹⁰⁴ Any legislation to deal with phoenix activity

¹⁰² Sandra Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (Report, Association of Business Recovery Professionals, August 2007); Vanessa Finch, 'Pre-Packaged Administrations and the Construction of Propriety' (2011) 11 *Journal of Corporate Law Studies* 1; Hal Lloyd, Maria O'Brien and Janna Robertson, 'Pre-Packaged Transactions in Administration — Strategy and Application' (2009) 9 *Insolvency Law Bulletin* 110; Nicholas Crouch and Shabnam Amirbeaggi, 'Pre-Packs: A Legitimate Means to Phoenix an Insolvent Company' (2011) 23(1) *Australian Insolvency Journal* 30; Mark Wellard, 'UK Pre-Pack Reforms: Pause for Thought in Australia' (2011) 23(2) *Australian Insolvency Journal* 12.

¹⁰³ See, eg, Commonwealth, *Parliamentary Debates*, Senate, 9 May 2012, 2884 (Mathias Cormann).

¹⁰⁴ Ian Ramsay and Geof Stapledon, 'Corporate Groups in Australia' (Research Report, Centre for Corporate Law and Securities Regulation, The University of Melbourne, 1998) 3. The prevalence of corporate groups was confirmed in 2010 by Sandra van der Laan and Graeme Dean, 'Corporate Groups in Australia: State of Play' (2010) 20 *Australian Accounting Review* 121, 126.

within corporate groups will impact business structures far beyond those against whom it is targeted.

A *The Phoenixing Act*

It appears that the government, keen to be taking action but anxious not to alarm the business community, has only tackled simple issues, the ‘low-lying fruit’. Pursuant to the Phoenixing Bill, it is indeed beneficial for ASIC to be given administrative powers to appoint a liquidator where a company is abandoned or deregistered, rather than having to apply to the court for permission to do so.¹⁰⁵ This reduces costs and speeds up the commencement of liquidation. The liquidator may take appropriate action more quickly against directors for breaches of directors’ duties, or to claw back voidable transactions under the *Corporations Act* pt 5.7B, div 2, where, for example, directors have transferred assets to other entities for less than their full value.¹⁰⁶

In addition, liquidation also allows employees access to GEERS. This was claimed as a major advantage when the Bill was released. However it should be noted that the Minister responsible for workplace relations may also exercise his or her discretion to allow access to GEERS where a company is not in liquidation, as the Hon Julia Gillard did when Minister, for the benefit of the employees of Coastal Express Pty Ltd,¹⁰⁷ National Parts Pty Ltd¹⁰⁸ and Drivetrain Systems International Pty Ltd.¹⁰⁹ The amendment to the law to be brought about by the *Phoenixing Act* is an improvement on the present situation as it will simplify and reduce the delays associated with placing a company into liquidation or in seeking ministerial approval, but it is an improvement of form rather than substance. It does not greatly improve the outcomes for ASIC, employees or other unsecured creditors.

In addition, under the present deregistration provisions of the *Corporations Act*¹¹⁰ ASIC is vested with the property of the company¹¹¹ and takes on the powers of the company or a liquidator in satisfying the company’s liabilities.¹¹² Prior to the amendment of these provisions, the ASC’s¹¹³ 1996 report into phoenix activity had found that:

¹⁰⁵ For example, ASIC applied to the court to place a company into liquidation for the benefit of employees in the case of On Ground Logistics Pty : ASIC, ‘ASIC Takes Steps to Protect Employee Entitlements’ (Press Release, 07-118, 4 May 2007).

¹⁰⁶ See, eg, *Corporations Act* ss 588FB (uncommercial transactions) and 588FDA (unreasonable director-related transactions).

¹⁰⁷ Julia Gillard, ‘Assistance for Employees of Coastal Express’ (Media Release, 20 December 2007).

¹⁰⁸ Julia Gillard, ‘Assistance for Employees of National Parts’ (Media Release, 22 February 2008).

¹⁰⁹ Julia Gillard, ‘Assistance for Employees from Drivetrain Systems International’ (Media Release, 10 March 2009).

¹¹⁰ *Corporations Act* pt 5A.1. The part has been substantially re-written from the *Corporations Law* (Cth) version. This was in part as a result of the recommendation the Australian Securities Commission (‘ASC’) that ‘a detailed examination of the s 574 program’s objectives and outcomes be undertaken with a view to addressing phoenix activity’: Darren Barlow, ‘Project One: Phoenix Activities and Insolvent Trading’ (Research Paper No 95/01, ASC, 13 May 1996) 75.

¹¹¹ *Corporations Act* s 601AD.

¹¹² *Ibid* ss 601AE–601AF.

¹¹³ The ASC was the predecessor of ASIC.

[i]t would appear that approximately 92% of Phoenix companies are deregistered under the ASC's section 574 program.

Effectively the ASC is unintentionally assisting Phoenix offenders to escape prosecution and detection by deregistering the company and closing off the trail. This is particularly the case in circumstances where debts may be many, but small and no creditor action is taken to place the company under administration.¹¹⁴

There is no data available from ASIC to determine whether ASIC exercises these powers to prosecute phoenix behaviour by the directors of deregistered companies. It would therefore appear that the *Phoenixing Act*, in providing ASIC with an administrative power to order the winding up of a company, aims to shift at least some of the responsibility for detecting and prosecuting phoenix activity from ASIC to a liquidator. However, where the deregistered companies are without assets, it is questionable whether liquidators will be willing to accept these appointments. The new legislation provides that in the absence of a liquidator willing to take the role, ASIC itself must appoint a liquidator.¹¹⁵

B The Similar Names Bill

The Similar Names Bill is a useful improvement if it deters the behaviour that it targets, but its limitations are clearly evident. It does nothing to prevent phoenix behaviour where a different name is used for the new company. Indeed, where a company has become notorious in an industry for non-payment of its creditors, its former directors may be compelled to start its successor under a completely different name to enable it to obtain supply of goods and services.¹¹⁶ The Similar Names Bill does nothing to prevent the incorporation of a new entity with a similar name to the failed company where a related party of a director of the failed company — for example a spouse, son or daughter — is appointed director instead. The banking of cheques payable to the previous entity would clearly be actionable as a misuse of position under the *Corporations Act* s 182(1) and the proposed legislation is not needed to prosecute such behaviour.

The Bill also does not impose liability on directors for the debts of the failed company, but only for the debts of the new entity,¹¹⁷ and only if that new company is not carrying on business.¹¹⁸ This seems anomalous as the phoenix activity has caused harm to the creditors of the failed company rather than the new one. The section imposes civil liability, rather than civil penalty or criminal

¹¹⁴ Barlow, above n 110, 75.

¹¹⁵ *Phoenixing Act* sch 1 item 1, inserting *Corporations Act* s 489EC(3).

¹¹⁶ An example of this is the liquidated Beaver Press Sales Pty Ltd, whose director, Robert Francis, was prosecuted by the Fair Work Ombudsman for failure to pay wages and annual leave entitlements: *Fair Work Ombudsman v Francis* [2011] FMCA 1005 (19 December 2011). It was alleged that Francis has commenced another business of the same nature on the same premises through another company — Goodcrowd Integrated Print Communications Pty Ltd — of which he was the sole director and majority shareholder.

¹¹⁷ Similar Names Bill sch 1 item 1, inserting *Corporations Act*, s 596AJ(1).

¹¹⁸ *Ibid*, inserting s 596AM(1)(b).

liability, through the use of the expression ‘[a] person is liable to discharge the liability of a company’.¹¹⁹

C *Phoenixing and Voluntary Administration*

Both the *Phoenixing Act* and the Similar Names Bill avoid the complex area of VA. Neither addresses the situation where a failed company has entered VA and the company has been rescued via a deed of company arrangement (‘DOCA’).¹²⁰ Saving the business is indeed the primary objective of VA. The *Corporations Act* s 435A provides that:

The object of [pt 5.3A] is to provide for the business, property and affairs of an insolvent company to be administered in a way that:

- (a) *maximises the chances of the company, or as much as possible of its business, continuing in existence; or*
- (b) if it is not possible for the company or its business to continue in existence — results in a better return for the company’s creditors and members than would result from an immediate winding up of the company.¹²¹

The mechanism by which phoenix activity is supposedly thwarted in VA is the requirement that the DOCA is voted on by creditors. If they are not satisfied with the deal they are being offered under the DOCA, creditors have the option to vote to have the company wound up¹²² and the company’s affairs are then placed in the hands of a liquidator. However, there is the possibility that phoenix activity may still be taking place where the vote on the DOCA by the creditors has been determined by either the controllers of the company in their capacity as creditors, or by other creditors who might have made secret arrangements to be paid by the controllers from the assets of the new entity. This is often the case in small family-owned companies, where related party votes may carry the DOCA through, even though some or all of the other creditors object to it. It is too early to say whether the resurrection of the well-known Chris and Marie’s Plant Farm Group, placed into administration on 7 November 2011 and returned to the hands of its owners on 24 December 2011 is one such company. Newspaper reports indicate that the votes of related parties were responsible for the acceptance of the DOCA and that non-related-party creditors are expecting to receive only 6 cents in the dollar.¹²³ Concerns of this nature are not new, and the issue was raised by in a 1998 ASC report into VAs.¹²⁴

¹¹⁹ Ibid, inserting s 596AJ(1).

¹²⁰ The DOCA records the compromise reached with creditors.

¹²¹ Emphasis added.

¹²² *Corporations Act* s 439C(c).

¹²³ Ben Butler, ‘Fury as Nursery to Repay Only 6¢ in Dollar’, *Sydney Morning Herald* (online), 11 January 2012 <<http://www.smh.com.au/small-business/managing/fury-as-nursery-to-repay-only-6162-in-dollar-20120111-1pu6d.html>>.

¹²⁴ Barry Cook, ‘A Study of Voluntary Administrations in New South Wales’, (Research Paper No 98/01, ASC, 1998) 22 [2.113], 39–40 [7.501].

This is not to suggest that the *Phoenixing Act* or the Similar Names Bill facilitate the phoenixing of companies placed into VA. Rather, they do not address the issue in any way. The *Corporations Act* s 600A already allows the court to set aside the decision of the second creditors' meeting on the DOCA where the outcome has been determined by votes cast by related entities. But, just like the other mechanisms already available to ASIC and other parties to deal with phoenix activity, such as the directors' duties provisions, there needs to be an application to the court. This is expensive and time-consuming, and creditors already facing non-payment of their debt may be concerned at investing money in such an application.¹²⁵ As a result, it is most likely only to be attempted by major unsecured creditors such as the ATO. For example, in *Woodings*,¹²⁶ a company which was subject to a DOCA was one of seven companies controlled by the same directors. The assets of each company had been stripped, leaving creditors, including the tax office, unpaid. The court used its powers to set aside the DOCA and order the company be wound up.¹²⁷

One advantage of the Similar Names Bill is that the directors face liability for the new company's debts, *unless* they have received an exemption from a liquidator or from the court, based on the liquidator's or court's belief that the person has acted honestly and having regard to all the circumstances, ought fairly to be exempt. The onus here, appropriately, is on the director to obtain such a dispensation. This sort of mechanism ought to be adapted to deal with the circumstances of phoenixing in the context of VA. After all, it is the directors who are asking for a second chance. Creditors are already to some extent out of pocket. Why should they be put to the additional expense of a court application under s 600A to overturn the DOCA?

D *Issues of Enforcement*

The government is urged to look at the phoenix company problem more broadly. It needs to ask whether the present directors' duties provisions are adequate or not. There seems to be a presumption that since phoenix activity is continuing, these laws must somehow be unable to tackle it, and therefore new legislation must be enacted. But the rarity of prosecutions may not be indicative of inadequacy if the issue is a lack of ASIC resources to take action. The passage of further legislation will make little difference to the incidence of phoenix activity if ASIC has no additional capacity to follow up breaches. Upon the introduction of the Phoenixing Bill, one Coalition member of the House of Representatives commented that

[t]he regulators are not fully utilising the existing powers available to them. Other issues include a lack of prosecution, underresourced regulators, insufficient follow-up on complaints, and inadequate penalties to act as a

¹²⁵ See, eg, *Khoury & Sons v Zambena Pty Ltd* (1999) 217 ALR 527, 543 [76] (Fitzgerald JA).

¹²⁶ (1994) 13 WAR 189.

¹²⁷ *Ibid* 203.

deterrent. In this context, the case for additional new ASIC powers seems exceptionally flimsy.¹²⁸

It is questionable whether ASIC is sufficiently well resourced to prosecute corporate misbehaviour in general. Since 2008, external administrators — receivers, administrators and liquidators — have filed reports with ASIC to indicate their suspicions of director misbehaviour.¹²⁹ These reports are then collated by ASIC and made public in a collated, de-identified format.¹³⁰ The data is presented in tables showing reports of suspected breaches of particular sections, including those outlined in Part IV above, and of those, where the liquidator holds evidence of wrongdoing.¹³¹ The external administrator reports do not specify whether those breaches relate to suspected phoenix activity. In the most recent statistics available, which cover 2010–11, external administrators alleged misconduct in 70.4 per cent of reports, or 14 387 instances.¹³²

Only general data is available as to what happened in relation to those reports. In the period 2010–11, external administrators held documentary evidence of misconduct for 3561 reports, but they considered that only 851 of those warranted further inquiry.¹³³ ASIC then requested supplementary reports for 257 of these,¹³⁴ in part based on the size of the deficiency of assets within the company.¹³⁵ The purpose of the supplementary report is to provide ASIC with more detail to see whether the reported conduct warrants further investigation.¹³⁶ This appears to suggest that if ASIC were given more resources, more of these reports of documented misconduct might be investigated.

To find more definite data, one must look to the annual reports. ASIC's 2009–10 annual report shows 23 criminal prosecutions, with 22 convictions and 12 perpetrators jailed.¹³⁷ In addition, ASIC 'completed 30 civil proceedings and obtained more than [AU]\$287 million in recoveries, costs and fines. ... ASIC was successful in 94% of civil litigation and 80% of criminal matters'.¹³⁸ ASIC also banned 70 company directors for insolvency-related offences, with 42 of these based on reports from liquidators who received Assetless Administration Fund ('AAF') funding.¹³⁹ ASIC's 2010–11 annual report notes 26 criminal proceedings

¹²⁸ Commonwealth, *Parliamentary Debates*, House of Representatives, 29 February 2012, 2360 (Scott Buchholz).

¹²⁹ Using Form EX01: ASIC, *Regulatory Guide 16 — External Administrators: Reporting and Lodging*, RG 16, 1 July 2008, sch B.

¹³⁰ See, eg, ASIC, 'Insolvency Statistics: External Administrators' Reports 1 July 2007–30 June 2010' (Report No 225, ASIC, December 2010). Misconduct was not reported in the data for 2007–08.

¹³¹ *Ibid* 32.

¹³² ASIC, 'Insolvency Statistics: External Administrators' Reports 1 July 2010 – 30 June 2011', (Report No 263, ASIC November 2011) 22 [42].

¹³³ *Ibid* 23 [46].

¹³⁴ *Ibid* [48].

¹³⁵ *Ibid*. Of the 594 reports which were not followed up, only 51 related to deficiencies of AU\$5 million or more.

¹³⁶ *Ibid* 22 [43].

¹³⁷ ASIC, 'A Year of Achievement: ASIC Annual Report 09–10' (Annual Report, ASIC, 7 October 2010) 16.

¹³⁸ *Ibid*.

¹³⁹ *Ibid* 37.

completed, 34 civil proceedings, 14 enforceable undertakings and 24 negotiated outcomes.¹⁴⁰

It must be recalled that these figures are not confined to reports of phoenix activity and subsequent ASIC actions against directors. Such data is not publicly available; although ASIC itself appears to know which prosecutions are related to phoenix activity. For example, in 2007, the ASIC Chairman Jeffrey Lucy issued a press release declaring that ASIC had ‘banned 40 directors for a total of 144 years who have engaged in misconduct following company failures and repeat phoenix activity’.¹⁴¹ It must also be stressed that this discussion of enforcement is not intended to suggest that ASIC has been derelict in its duty to prosecute corporate misbehaviour in general or phoenix activity in particular. Rather, it seeks to highlight the problem where a regulator with a wide range of responsibilities is charged with the detection and enforcement of behaviour which closely mimics legal behaviour. Any changes to the law or regulatory arrangements should therefore be predicated on alleviating the detection and enforcement burden.

For example, in terms of enforcement of the law, the terms under which funding may be requested from the AAF may need to be revisited. The aim of the fund is to overcome the reluctance of liquidators to take action due to financial constraints. However, one of the AAF funding criteria is that an initial report¹⁴² must be lodged by a liquidator.¹⁴³ The scheme therefore relies on action taken by a liquidator in the first place. Funding, which is capped, is only available for investigations where *Corporations Act* s 206F director-banning proceedings may be appropriate, or where court proceedings for serious misconduct pursuant to the *Corporations Act* may be warranted.¹⁴⁴ While the *ASIC Regulatory Guide 109* indicates that ‘[a] particular focus of the AA Fund is to curb fraudulent phoenix activity’,¹⁴⁵ it is not available for actions for the recovery of assets,¹⁴⁶ which is the liquidator’s primary responsibility.¹⁴⁷ Moreover, funding is only provided if the initial report indicates sufficient evidence exists to support the allegations made.¹⁴⁸ This is surely a ‘chicken and egg’ argument: access to the fund depends on a liquidator of a company, which by definition is assetless, being willing to make investigations at their own expense to come up with the evidence sufficient to support their application for funding. It was this very reluctance on the part of liquidators to expose themselves to personal expense that the AAF was set up to overcome.¹⁴⁹

¹⁴⁰ ASIC, ‘Annual Report 2010–11’ (Annual Report, ASIC, 10 October 2011) 75 (‘ASIC Annual Report 2010–11’).

¹⁴¹ ASIC, ‘Phoenix Crackdown Reaps Results’ (Media Release, 07-05, 8 January 2007).

¹⁴² *Corporations Act* s 533.

¹⁴³ ASIC, *Regulatory Guide 109 — Assetless Administration Fund: Funding Criteria and Guidelines*, RG 109, 26 November 2009, RG 109.19 (‘*ASIC Regulatory Guide 109*’).

¹⁴⁴ *Ibid* RG 109.20.

¹⁴⁵ *Ibid* RG 109.4.

¹⁴⁶ *Ibid* RG 109.21.

¹⁴⁷ *Corporations Act* s 478(1)(a).

¹⁴⁸ *ASIC Regulatory Guide 109*, above n 143, RG 109.22.

¹⁴⁹ It is difficult to obtain the amount still unspent in the AAF in 2012 but the ASIC Annual Report 2010–11 indicates that AU\$3.45 million was available for allocation in that year and AU\$2.279 million was actually paid: ASIC Annual Report 2010–11, above n 140, 78. However, the Report states that the funding was fully utilised: at 82.

E *Possible Areas of Legislative Reform*

If it is concluded that the present legislation is inadequate, that inadequacy must be carefully identified. The present *Corporations Act* s 596AB would be an obvious target for revision, given its lack of use and the extensive criticism of its intention requirement. The government should consider reintroducing the provision as a civil penalty breach. This possibility was raised in the early days of the House of Representatives' debate of the Corporations Law Amendment (Employee Entitlements) Bill 2000 (Cth).¹⁵⁰ The Hon Kelvin Thomson said:

I understand that the government drafted the new section 596AB as a criminal offence, thus it was considered appropriate that the actual intention of a director be proved. However, because it is a criminal offence, not only must the actual intention of the director be proved but also it must be proved beyond any reasonable doubt. It was not necessary that section 596AB be drafted in that particular way. To compare again section 596AB with the insolvent trading provisions, section 588G is a civil penalty provision, which means not only is there an objective or reasonable person test but also that it needs to be proved on the balance of probabilities. A director can still be guilty of a criminal offence if it can be shown that the director contravened the provision knowingly, intentionally, recklessly, dishonestly or with the intention to deceive or defraud. ...

The contravention of section 596AB could still be a criminal offence if breached with the requisite intention, but as a civil penalty provision employees would have a greater likelihood of succeeding in recovering compensation from directors.¹⁵¹

In addition, the government should look overseas more widely for solutions to the problem. The Similar Names Bill is a good start but is easily avoided by choosing a different name. In relation to the basic form of phoenixing, the government should note that Ireland requires directors who have run companies against whom adverse liquidators' reports have been lodged to ensure that a large amount of equity capital is invested in the new company or to prove in court why they should not be required to do so.¹⁵² This reverse onus relieves the detection and compliance burden on their regulator.¹⁵³ In the case of a public limited company, it is at least £100 000 and in the case of any other company, it is at least £20 000, and these amounts must be fully paid up in cash.¹⁵⁴ It is open to the directors to prove that they have 'acted honestly and responsibly in relation to the conduct of the affairs of the company and that there is no other reason why it would be just and equitable that they should be subject to the requirements imposed by this section'.¹⁵⁵

¹⁵⁰ Commonwealth, *Parliamentary Debates*, House of Representatives, 9 March 2000, 14301–2 (Kelvin Thomson).

¹⁵¹ *Ibid.*

¹⁵² *Companies Act 1990* (Ireland) s 149.

¹⁵³ *Ibid* s 150; *Company Law Enforcement Act 2001* (Ireland) s 56.

¹⁵⁴ *Companies Act 1990* (Ireland) s 150(3).

¹⁵⁵ *Ibid* s 150(2)(a).

This may not be the whole answer, of course. Unless the company was required to hold this share capital in trust in some way, it could be expended and lost in the operations of the business, and creditors would be no better off. A personal guarantee might work better, except that it could be defeated by the personal bankruptcy of the individual director. Asking for the payment of a bond, to be held by ASIC, may elicit complaints about removing scarce capital from the business, yet it should be remembered that in 2010 the Commissioner of Taxation's ability to require security bonds to be payable by suspected phoenix companies was strengthened. This sort of requirement therefore is not without precedent, and these options, including the Irish legislation, should be examined by the government.

The issue of mandatory capitalisation of all companies also needs to be addressed. One of the recommendations of the *2009 Phoenix Proposals Paper* was to 'allow the corporate veil to be lifted where a company sets up a subsidiary with insufficient capital to meet the debts that could reasonably be expected to arise.'¹⁵⁶ This sort of reform would be beneficial for the sophisticated form of phoenix activity within corporate groups, where subsidiaries are set up undercapitalised but have their operations financed by credit, often secured, from the parent company. However, this would be problematic, given the vagueness of what amounts to sufficient capital, whether such capital needs to be maintained throughout the life of the company or is only required at its inception, and so forth. In any event, the lack of assets in a subsidiary may be attributable to the parent company using its domination of the subsidiary to transfer value to itself, through excessive dividends, overpricing of intra-company sales and underpricing of purchases, and similar mechanisms, rather than a lack of initial capital. Internationally, capitalisation is a vexed issue, in terms of the companies to which it applies, setting adequacy levels and policing its maintenance,¹⁵⁷ and the trend is away from mandatory capitalisation rules rather than towards them.¹⁵⁸

One approach which helps to overcome these issues is the subordination of parent company debt. Both the United States and Germany have laws subordinating parent debt, and interestingly, these two countries treat this problem in different ways.¹⁵⁹ In the US, the equitable subordination doctrine was codified in 1978.¹⁶⁰ It allows a court to subordinate the claim or interest of a creditor, being a shareholder or affiliated entity, who has acted inequitably.¹⁶¹ Thus, its basis is a

¹⁵⁶ *2009 Phoenix Proposals Paper*, above n 8, vii.

¹⁵⁷ See, eg, John Armour, 'Legal Capital: An Outdated Concept?' (2006) 7 *European Business Organization Law Review* 5; Jennifer Payne, 'Legal Capital in the UK following the *Companies Act 2006*' in John Armour and Jennifer Payne (eds), *Rationality in Company Law: Essays In Honour Of D D Prentice*, (Hart Publishing, 2009) 123; Jennifer Payne, 'Legal Capital and Creditor Protection in UK Private Companies' (2008) 5 *European Company Law* 220.

¹⁵⁸ The newly introduced *Unternehmersgesellschaft* [entrepreneurial company] is a recognition of this trend. It has a mandatory minimum capital of €1.00. It was brought in by *Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen* [Law for the Modernisation of the GmbH and to Stop Its Misuse] (Germany) 28 October 2008, BGBI I, 2008, 2026 ('*MoMiG*').

¹⁵⁹ Other countries with equitable subordination rules include Italy, Spain and Austria.

¹⁶⁰ 11 USC § 510 (2012); *Bankruptcy Reform Act 1978*, Pub L No 95-598, 92 Stat 2549.

¹⁶¹ The National Bankruptcy Review Commission had proposed that insider claims be automatically subordinated: National Bankruptcy Review Commission, *Report of the Commission on the*

combination of enterprise principles and fiduciary concepts, and does not rely upon satisfying the requirements of ‘piercing the veil’ jurisprudence.¹⁶² Its origins lie in the leading 1939 cases of *Taylor v Standard Gas & Electric Co*¹⁶³ (‘*Deep Rock*’), and *Pepper v Litton*.¹⁶⁴ Prior to this time, debt extended by a shareholder could only have been actioned under fraudulent conveyance law.¹⁶⁵ In *Deep Rock*, the Supreme Court based its findings upon the ‘equitable principle that the doctrine of the corporate entity, recognized generally and for most purposes, will not be regarded when so to do would work fraud or injustice’.¹⁶⁶ In *Pepper v Litton*, the Court said that ‘[i]n the exercise of its equitable jurisdiction the bankruptcy court has the power to sift the circumstances surrounding any claim to see that injustice or unfairness is not done in the administration of the bankrupt estate.’¹⁶⁷

In addition, US courts have the power to re-characterise debt as equity in certain circumstances, even where the shareholder has not acted inequitably.¹⁶⁸ The power of courts to re-characterise debt as equity arguably arises from the discretion given to courts by the 1978 codification to subordinate other claims as circumstances warranted.¹⁶⁹ Frequently, the issue is decided as recharacterisation because it is unclear whether a debt actually exists, due to a lack of formalities surrounding the provision of the additional funds to the company.¹⁷⁰

In 2008, Germany substantially overhauled its subordination laws.¹⁷¹ Prior to 2008, loans by shareholders to GmbH companies were deemed to be ‘substitutes for equity’ and treated as equity if they were granted in the course of a ‘crisis’ of a company or, if granted before the crisis began, they were not immediately withdrawn when it did begin.¹⁷² The rationale for this rule was that shareholders have decided to support the company financially during its difficulties and allow it to continue, and in these circumstances, they should be ‘prevented from

Bankruptcy Laws of the United States, H R DOC No 93-137 (1973). This proposal was not adopted.

¹⁶² See Phillip I Blumberg, ‘The Increasing Recognition of Enterprise Principles in Determining Parent and Subsidiary Corporation Liabilities’ (1996) 28 *Connecticut Law Review* 295, 328.

¹⁶³ 306 US 307 (1939).

¹⁶⁴ 308 US 295 (1939). See further Adolf A Berle Jr, ‘The Theory of Enterprise Entity’ (1947) 47 *Columbia Law Review* 343, 348–50.

¹⁶⁵ See Douglas G Baird, ‘Legal Approaches to Restricting Distributions to Shareholders: The Role of Fraudulent Transfer Law’ (2006) 7 *European Business Organization Law Review* 199.

¹⁶⁶ 306 US 307, 324 (1939). See also David A Skeel and Georg Krause-Vilmar, ‘Recharacterization and the Nonhindrance of Creditors’ (2006) 7 *European Business Organization Law Review* 259, 262–4.

¹⁶⁷ 308 US 295, 307–8 (1939).

¹⁶⁸ Skeel and Krause-Vilmar, above n 166, 265.

¹⁶⁹ The relevant provision is 11 USC § 510(c)(1) (2012). However, Skeel and Krause-Vilmar question this basis for the exercise of the power: *ibid* 266.

¹⁷⁰ For a discussion of other factors which may be considered, see *Benjamin v Diamond (Re Mobile Steel Co)* 563 F 2d 692 (5th Cir, 1977).

¹⁷¹ *MoMiG*. See Dirk A Verse, ‘Shareholder Loans in Corporate Insolvency – A New Approach to an Old Problem’ (2008) 9 *German Law Journal* 1109, 1112–21.

¹⁷² The relevant provisions were: *Gesetz betreffend die Gesellschaften mitbeschränkter Haftung* [Act concerning Companies with Limited Liability] (Germany) 20 April 1892, RGBl, 1892, 477, §§ 32a–32b; *Insolvenzordnung* [Insolvency Act] (Germany) 5 October 1994, BGBI I, 1994, 2886, § 135 (‘*Insolvency Act (Germany)*’); *Gesetz über die Anfechtung von Rechtshandlungen eines Schuldners außerhalb des Insolvenzverfahrens* [Law concerning the Contestability of Legal Acts of a Debtor outside of Insolvency Proceedings] (Germany) 21 July 1879, RGBl, 1879, 277 § 6.

speculating at the expense of creditors.’¹⁷³ Although there was no need to prove inequitable conduct on the part of the lender, problems arose in defining ‘crisis’. Post 2008, the subordination rules have been moved from the GmbH legislation to the *Insolvency Act (Germany)*,¹⁷⁴ thus extending it to stock corporations. In addition, the subordination rules apply to all loans by shareholders to the company made within one year prior to, or after filing for insolvency,¹⁷⁵ and not just those given or maintained during the company’s financial crisis. Certain exceptions apply.¹⁷⁶ This bright line rule has the advantage of simplicity, although it may cause some injustice where the company’s insolvency has been precipitated by an external cause beyond the control of the company’s controllers.

Another means by which corporate groups can be discouraged from engaging in phoenix activity is the introduction of contribution orders. New Zealand and Ireland both allow for courts to make orders against solvent holding companies to contribute to the debts of insolvent subsidiaries where it is just and equitable.¹⁷⁷ This is determined in accordance with specified factors.¹⁷⁸ In Ireland, the legislation provides that ‘[n]o order shall be made ... unless the court is satisfied that the circumstances that gave rise to the winding up of the company are attributable to the actions or omissions of the related company.’¹⁷⁹ The connection between the culpability of the related company and the demise of the insolvent company is expressed in much stronger terms than its New Zealand equivalent.¹⁸⁰ Given the deliberate nature of phoenix activity as seen in cases like *Ramsey*¹⁸¹ noted above, courts should have no difficulty in piercing the corporate veil to require the parent company to pay the subsidiary’s debts if legislation like this were introduced in Australia.

VII Conclusion

The federal government is right to accept its responsibility to tackle phoenix activity, which hurts its own revenue streams as well as the economic wellbeing of employees and creditors of companies. While the *Phoenixing Act* and the *Similar Names Bill* are unlikely to do any harm, these measures fall far short of what is required to significantly overcome the problem. The existing directors’ and officers’ duties clearly deal with the types of actions typically taken in

¹⁷³ Verse, above n 171, 1114.

¹⁷⁴ *Insolvency Act (Germany)* §§ 39(1) n 5, (4)–(5) (as amended).

¹⁷⁵ *Ibid* §135(1) n 2.

¹⁷⁶ The rules do not apply to shareholders who are not directors and who do not hold more than 10 per cent of the company’s registered capital; or new investors who are attempting to rescue the company. These exceptions also applied under the old rules.

¹⁷⁷ *Companies Act 1993* (NZ), s 271(1); *Companies Act 1990* (Ireland) s 140.

¹⁷⁸ The factors are specified under *Companies Act 1990* (Ireland) s 140(2) and *Companies Act 1993* (NZ) s 272(1). The factors under s 272(1) are: the extent to which the related company took part in the management of the company in liquidation; the conduct of the related company towards the creditors of the company in liquidation; the extent to which the circumstances that gave rise to the liquidation of the company are attributable to the actions of the related company; and such other matters as the court thinks fit.

¹⁷⁹ *Companies Act 1990* (Ireland) s 140(3).

¹⁸⁰ *Companies Act 1993* (NZ) s 272(1)(c).

¹⁸¹ (2011) 198 FCR 174, 176–7 [3].

phoenix circumstances, and carry harsh penalties, including imprisonment for intentionally dishonest or reckless breaches. Serious thought needs to be given to why these laws are not sufficient, or whether there are issues of enforcement that should first be addressed.

This article has argued that now is the time for a broader examination of the options available to deal with phoenix activity. Failing to do so while there is a groundswell of concern would be an opportunity lost. New legislation may indeed assist in deterring phoenix activity and in prosecuting when it occurs. The avoidance of employee entitlements should be dealt with by a re-working of the never-used *Corporations Act* s 596AB. In addition, directors of failed companies should have the onus of showing why they should be given the privilege of running another limited liability entity, rather than the onus being on ASIC to seek their banning. While the imposition of a reverse onus inevitably prompts the retort that business enterprise will be hindered, the Similar Names Bill is essentially doing just that. However, it is absurd to limit such a requirement to the easily-avoidable circumstance of having a similar name to the failed company.

In addition, the Government must accept the advice in the *2009 Phoenix Proposal Paper* that phoenix activity is not limited to successor companies, but also occurs within corporate groups. The *Phoenixing Act* and the Similar Names Bill do nothing in these circumstances. A proper inquiry needs to be made into the various mechanisms available internationally which pierce the corporate veil to make parent companies liable to contribute to the debts of their insolvent subsidiaries or to subordinate repayment of subsidiary debts owed to them until external creditors are paid.