

Insolvency practices to face scrutiny



Kate Carnell, Small Business Ombudsman

A formal review into how the insolvency sector deals with failing small businesses is under way after being announced in October by Small Business Ombudsman Kate Carnell and former Nationals senator John “Wacka” Williams.

Carnell says the success rate of restructuring businesses under external administration could be improved, and she called for banks, lenders, lawyers and insolvency firms to contribute to the inquiry. She says there are serious questions over the current insolvency system and whether it encourages practitioners to restructure and turn a business around rather than send it into administration.

In Australia during 2018-19, more than 8000 businesses entered into external administration.

Limited knowledge of insolvency process



Andrew Spring, Jirsch Sutherland Partner

Jirsch Sutherland Partner Andrew Spring says insolvency practitioners work within an industry that “no one wants to understand until they find themselves subjected to it”. Because of this, he says, general knowledge of the insolvency process is limited.

“What people need to understand is that insolvencies are not created by insolvency practitioners; we are just here to try and clean up the mess,” he says.

Jirsch Sutherland National Managing Partner Bradd Morelli agrees that people often blame the insolvency practitioner when it’s often not their fault. One problem, he says, is that small-business owners are often so close to the business, they leave issues until it’s too late to seek help.



Jirsch Sutherland National Managing Partner Bradd Morelli

“Often there might have been options but by the time they seek help, those options are off the table,” he says. “No one is obliged to act on advice we give but if early help is sought, then at least businesses would have an understanding of options and could make an informed decision.”

Meanwhile, Spring adds that the Australian insolvency legislation is still relatively new in comparison to more established areas of commercial life, such as contract law. “An investigation that is designed to consider the process and how it is administered – with the intended outcome being to improve the interactions that occur between insolvency practitioners and the debtor’s stakeholders – can be a good thing, if that is the intention,” he says. “If it is a witch hunt then that is another matter altogether.”

Terms of reference

The review’s terms of reference state that the inquiry will examine:

- the existing insolvency system through the experience of small business;
- the degree of transparency of the governance, processes and costs of practitioners including legal advisers, valuers, investigating accountants, administrators, receivers and liquidators;
- how the insolvency of a small or family business may lead to bankruptcy for the owners; and
- how the framework affects the practices and fees of insolvency practitioners.

The final report will consider how small-business operators are treated during the insolvency process, including the governance and methods used by valuers, administrators, liquidators and lawyers. The practices and costs of the insolvency sector will also be examined.

The Australian Restructuring Insolvency and Turnaround Association (ARITA) has dismissed the inquiry as a narrow-focused media stunt. CEO John Winter says ARITA plans to form its own Financial Recovery Law Reform Commission, which will be led by an eminent group of commissioners it would appoint to conduct a review of the insolvency regime.

Spring says the terms of reference for the review are difficult to judge because every company's circumstances are unique. "How can there be typical outcomes; how can you assess how liquidators maximise returns or judge if costs were appropriate," he asks. "It sounds like the terms of reference can only be applied to specific examples. And if the assessment is based on specific examples, then you run the risk of creating an outcome based on a small sample size."

Insolvency practitioners are here to help, Spring says, and will generally have an independent, no obligation and confidential chat for no charge.

"Most insolvency practitioners have spent more than 10 years training to be registered," he says. "They operate under a significant level of regulation and in a transparent environment. Their role is to help those that find themselves in a form of financial distress escape the downward spiral and move on with their lives. They provide transparency to stakeholders and the opportunity to get certainty on credit relationships. And they operate with the dual responsibility of realising and distributing assets, as well as investigating the affairs of the debtor for the public interest.

"If you are concerned about your business' performance, why wait?"

The review will present an interim report on December 11 and a final one by February 2020.