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Eye of the phoenix

Anna Smith of K&L Gates looks at the latest developments in the campaign to combat illegal phoenix activity.

WHAT IS ILLEGAL phoenix activity and why is it a problem?

Recent studies have shown that illegal phoenix activity is rife. It has resulted in direct costs to businesses, employees and the Government of \$2.85 billion to \$5.13 billion in the 2015/16 financial year alone.

The Australian Taxation Office (ATO) describes illegal phoenix activity as "...when a new company is created to continue the business of a company that has been deliberately liquidated to avoid paying its debts, including taxes, creditors and employee entitlements."

This type of activity negatively affects a range of stakeholders, including unpaid suppliers and contractors, competitors (over whom the phoenixed company can gain a competitive advantage as a result of not having to pay its debts), employees (who may miss out on unpaid wages, superannuation and other entitlements) and the government (as a result of loss of government revenue and increased monitoring and enforcement costs).

Although there are a number of existing provisions within the Corporations Act 2001 (Cth) (Corporations Act) which can be against perpetrators of this illegal phoenix activity it is clear that more needs to be done to combat this behaviour.

Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019

On 14 February 2019, the Senate referred the Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019 (the Bill) to the Senate Economics Legislation Committee for inquiry and report by 26 March 2019.

The Bill introduces a range of proposed amendments to the Corporations Act aimed at combatting illegal phoenixing.

One of the key amendments proposed is the introduction of the concept of the "creditor-defeating disposition" which is a disposition:

- where the consideration payable to the company for the disposition is less than the market value of the property, or the best price reasonably obtainable for the property, having regard to the circumstances existing at that time; or
- which has the effect of:
- preventing the property from becoming available for the benefit of the company's creditors in the winding-up of the company; or
- hindering, or significantly delaying, the process of making the property available for the benefit of the company's creditors in the winding-up of the company.

Under the Bill, these "creditor-defeating dispositions" will be voidable against a subsequently-appointed liquidator of the company if made while the company was insolvent or within the 12 months preceding the external administration of the company.

The Bill also introduces new (civil and criminal) offences for company officers that fail to prevent the company from making creditor-defeating dispositions and others (such as "pre insolvency advisors") that facilitate a company making a creditor-defeating disposition.

How can you avoid becoming a victim of illegal phoenix activity?

You can protect your business by doing your due diligence before entering into a commercial arrangement such as:

- undertaking an ASIC company search (via ASIC Connect: www.asic.gov.au) for a small fee, to ensure the company is registered and to check that it is not under

external administration. You can also conduct a free search to confirm the entity's ABN is valid: www.abr.business.gov.au

- asking for references
- doing a credit check, and
- searching online for any adverse media reports relating to the company or its directors.

There are also some warning signs which businesses can look out for which may indicate a company is involved in illegal phoenix activity. For example:

- a company offering significantly lower pricing or prices that are lower than market value
- the directors of a company have previously been involved with liquidated entities, and
- a company requesting that payments are made to a new company or subtle changes are made to the invoicing entity (ie name, ACN or ABN).

Reporting illegal phoenix activity

Suspected illegal phoenix activity can be reported to the ATO either online (<https://www.ato.gov.au/reportphoenixactivity>) or by calling the ATO's phoenix hotline on 1800 807 875. ■

For more information about issues relating to illegal phoenix activity please contact Anna Smith, Special Counsel at K&L Gates (anna.smith@klgates.com). This article is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer.

