

Corporations Law Amendment (Employment Entitlements) Act 2000 Solving the Insolvency Dilemma?

Adrian Fong

*We all sat down and at seven o'clock he rolled up and said,
'Well at 10 o'clock the administrator comes in — he takes over.
You're all sacked, and I've got no money to pay you'.*

Roy Lamoon, Oakdale miner.

THIS ALL-TOO-FAMILIAR SCENARIO has plagued our industrial life. In 1998 there was the much publicized waterfront dispute and more recently the hardships faced by sacked workers at National Textiles in the New South Wales Hunter Valley. Media attention to such events, highlighted especially in times of an economic boom, have forced politicians to sit up and take notice.

The new changes to the Corporations Law, *Corporations Law Amendment (Employee Entitlements) Bill* are a clear indication that Parliament is intent on reforming the protection of employee entitlements in insolvency situations. Employment Minister, Peter Reith, described the amendments as recognition of the primary responsibility that employers have to meet their employees' entitlements.

In summary, the amendments:

- ▶ Introduce a new offence to penalize persons who deliberately enter into arrangements or transactions for the purpose of avoiding payment of employee entitlement;
- ▶ Allow a court to order persons in breach of the new offence provision to pay compensation to employees who have suffered loss or damage because of the arrangements or transactions;
- ▶ Deem that a company incurs a debt for the purposes of the insolvent trading provisions when it enters into an uncommercial transaction — thereby extending the current duty on directors not to engage in insolvent trading.

Under section 596AB, a criminal offence is committed where a person enters

into an arrangement or transaction with the intention of preventing or significantly reducing the recovery of employee entitlements. A fine of up to \$100,000 or a prison sentence of up to 10 years is liable.

The object of this section is to deter the misuse of company structures and of other schemes to avoid payments to employees (that they are entitled to prove on the liquidation of the employer). One criticism of this provision is that the criminal standard of proof, combined with the need to prove intent, required for a prosecution would mean few successes.

Section 596AC has increased the scope for recovery of employee entitlements during liquidation. If an employee suffers loss because a person enters into an arrangement or transaction to avoid the payment of employee entitlements, the employee or the liquidator may seek to recover compensation from that person.

A breach of this provision will constitute a civil offence. It will only be necessary to satisfy the court that there was a breach on the balance of probabilities. An obstacle may be the lack of resources an employee or a liquidator has to pursue an action.

The last significant amendment is the proposed extension of the insolvent trading prohibitions imposed on directors so as to cover 'uncommercial transactions'. An uncommercial transaction is generally defined under the *Corporations Law* as one that a reasonable person would not have entered into having regard to the benefits and detriments to the company, respective benefits to the other parties to the transaction and any other parties to the transaction and any other relevant matters. Currently uncommercial transactions are avoidable by application of

the liquidator. However there is no duty on directors not to engage in an uncommercial transaction (for example conferring a financial benefit to another party) which doesn't involve the incurrence of a debt where the company is or becomes insolvent, and no penalty for doing so. The amendment will impose this new duty on directors.

The argument submitted by the Law Council was that the extension of the insolvent trading provisions may adversely affect the proper functioning of boards of directors and was inconsistent with the business judgment rule. Similarly, the Australian Institute of Company Directors objected on the basis that it introduces further potential for directors to be judged with the benefit of hindsight for decisions taken with diligence and in good faith. Whether a director should be excused for bad management is questionable. However, directors of companies should be aware that this amendment widens the scope of directors' liabilities. They will need to be mindful of the basis on which they enter into transactions, to ensure they have a reasonable basis for doing so at all times.

It is not clear whether these amendments alone will have any impact on how companies organize their affairs in relation to employee entitlements. Further changes may be introduced, as labor members' and Senate reports concluded that the amendments only focused on penalising directors rather than protecting employee entitlements. It was also recommended that the operation of the legislation be reviewed after 12 months. However, such changes would be subject to the developments of the current national Employee Entitlement Support Scheme fund established on an interim basis by the Federal Government and its consideration of a compulsory employer insurance scheme initially proposed by the ALP. ■

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