
Sunlight as the disinfectant for phoenix activity

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Over more than two decades, various inquiries initiated by government have struggled to come up with a definition of phoenix activity, as a step towards proscribing this troublesome and costly behaviour. At present, therefore, those who engage in this activity have only been brought to account by a patchwork of provisions spanning taxation, labour and corporate law. This article takes a lateral approach to tackling the phoenix issue by suggesting some structural and practical changes to the present landscape. These are based on “sunlight” – greater collection of information at the time of incorporation, sharing of that data between regulators, and public availability of information for those who risk being affected by phoenix activity. While these suggestions have recently found favour with two government-initiated inquiries, Australia’s pro-innovation, anti-red tape government has yet to publicly endorse or act upon these recommendations.

INTRODUCTION

In simple terms, phoenix activity involves the closing down of one failed company and the transfer of its business, but not its debts, to another company. This is the consequence of the fact that the failed company, as a separate legal entity, is solely responsible for payment of those debts. Its controllers are free to start another company and to buy from the failed company assets that are useful to the new company. In some instances, the failure of the first company is either brought about deliberately or used as an opportunity to improperly benefit the new company through the transfer of assets at an undervalue. This breaches directors’ duties or other fraud-related laws, and is commonly referred to as illegal or fraudulent phoenix activity. However, it is arguable that phoenix activity engaged in by what might be termed “inept serial entrepreneurs” – those who repeatedly start and fail at business enterprise – is equally a problem.

The identification of phoenix activity as a significant issue for revenue authorities, employees, unsecured creditors, competitors and others is more than two decades old. Nonetheless, despite a range of measures that appear to deal with phoenix activity, the latest PWC research confirms that the issue has not gone away. This suggests that different approaches should be considered.²

Phoenix activity, whether of the illegal or inept serial entrepreneur variety, might be said to thrive for the following reasons. First, it is largely invisible because there is little scrutiny of transactions surrounding insolvency and no attendant public condemnation of company controllers for the failure of their business. Second, it is easy to do because the liquidation of the failed company and creation of a second or twenty-second company is straightforward. Third, it is profitable, because the cost of liquidating a company and starting another one may be dwarfed by the amounts of debts to employees, revenue authorities and unsecured trade creditors – sometimes in the hundreds of thousands of dollars – that can be shed by the process.

This article tackles the phoenix issue by trying to undermine these incentives towards this behaviour, while at the same time not interfering unduly with the legitimate and worthy rescue of a failed business. It maintains that Louis Brandeis’ “sunlight” – in this instance, comprehensive, readily available information about companies and their directors – will help to overcome the invisibility and ease with which phoenix activity operates. While greater transparency has recently found favour with

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² This article is part of the much larger work of the author, Helen Anderson, and other researchers: Professor Ian Ramsay, Professor Ann O’Connell and Associate Professor Michelle Welsh: see <<http://law.unimelb.edu.au/centres/cclsr/research/major-research-projects/regulating-fraudulent-phoenix-activity>>.

two government-initiated inquiries, their recommendations are yet to be publicly endorsed or acted upon. In making the case for greater visibility of phoenix activity, there must be a recognition of the political climate in which they are made, including the 2015 pro-innovation announcements and anti-red tape stance of the Coalition Government. Moreover, in the background is a broader debate about new mandatory data retention legislation³ – allowing access to so-called “metadata” – amid privacy concerns over the availability of people’s phone records.⁴

The section of the article entitled “Background” provides the context of the discussion. It outlines the problem of phoenix activity and how it has been treated to date. It questions why phoenix activity continues to exist despite widespread condemnation by governments, regulatory agencies and others, and despite a suite of measures that ought to deter would-be abusers of the business rescue process.

The section “Gathering data” considers the gathering of data at the time of incorporation. Surprisingly little information, none of it verified, is collected when a company is incorporated, and this section suggests a range of improved mechanisms to overcome this.

“Sharing data amongst regulators” looks at information flows between regulators and what might be hindering them.

The section of the article entitled “Making data available to liquidators, superannuation funds and the public” examines access to regulator-held data as a means by which the liquidators can better perform their roles and through which creditors and superannuation funds can protect against the consequences of phoenix activity. This section also comments on the government’s proposal to privatise the Australian Securities and Investments Commission (ASIC) registry and Treasury’s bid for ASIC to be funded by industry.

“Conclusion” states that while greater transparency is not the sole answer to a problem as complex as phoenix activity, it has the capacity to undermine the incentives towards this strategy to avoid debts.

BACKGROUND

To begin, the enormous cost of phoenix activity to the economy must be recognised. In 2012, PriceWaterhouseCoopers estimated lost employee entitlements of between \$191,253,476 and \$655,202,019 annually.⁵ That report also estimated losses generally to business to be between \$1,784,338,743 and \$3,191,142,300 annually.⁶ While the reliability of these figures is not unquestioned,⁷ they nonetheless indicate the scope of the losses that are associated with phoenix activity.

The wide range of these estimates reflects the difficulty in quantifying illegal phoenix activity, which in part is caused by problems differentiating the legal and illegal forms of this behaviour. It is not illegal for people to close failed companies they have controlled, then incorporate a new company which buys the assets or business of that failed company. Indeed, this may provide the best outcome for the failed company’s creditors and employees. Yet our regulators may be expected to provide protection against the illegal versions of phoenix activity and to enforce relevant breaches of the law. ASIC, as the corporate regulator, enforces breaches of directors’ duties and disqualifies directors who have been involved in multiple failed companies. The Australian Taxation Office (ATO) enforces tax laws including those where employment taxes and superannuation have not been remitted. The Fair

³ *Telecommunications (Interception and Access) Amendment (Data Retention) Act 2015* (Cth).

⁴ See, eg, Hannah Francis, “Dozens of government agencies request access to citizen metadata without warrants”, *Sydney Morning Herald*, 19 January 2016, <<http://www.smh.com.au/technology/technology-news/dozens-of-government-agencies-request-access-to-citizen-metadata-without-warrants-20160119-gm8uql.html>>.

⁵ PriceWaterhouseCoopers, “Phoenix Activity: Sizing the Problem and Matching Solutions: Report Prepared for the Fair Work Ombudsman” (PWC, 2012) iii.

⁶ PriceWaterhouseCoopers, n 5.

⁷ H Anderson, A O’Connell, I Ramsay, M Welsh and H Withers, *Quantifying Phoenix Activity: Incidence, Cost, Enforcement: Major Report* (Centre for Corporate Law and Securities Regulation, 2015).

Work Ombudsman (FWO) can seek a penalty from the court against controllers of companies which have not paid wages and other entitlements. Each has a role to play where phoenix activity is suspected.⁸

However, theoretically at least, creditors are meant to protect themselves against the risk that they will not be paid what they are owed by a corporate debtor. They are alerted by the words “limited” or “proprietary limited” to the fact that the company, not its shareholders or its controllers, is responsible for its own debts.⁹ If the company enters liquidation lacking assets to pay outstanding debts, unsecured trade creditors will share *pari passu* behind priority creditors in the company’s winding up.¹⁰ To cope with this exposure to the risk of loss, creditors are expected to protect themselves through *ex ante* measures, such as seeking security or charging more for the products or services they supply. Their ability to do so depends upon the strength of their bargaining power with the company and most importantly upon the quality of the information they possess about the likelihood of loss. If a building sub-contractor knows that those who control a building company have a long history of being associated with companies that do not pay their bills,¹¹ it may demand pre-payment or security, or decide not to contract at all.

Employees are also vulnerable creditors upon their employer’s insolvency.¹² Information about the prospective employer’s prior corporate history is important in deciding whether to take that particular job. As creditors, the ATO and state revenue authorities do not enjoy the option of not doing business with a company whose controllers have a past record of non-payment, but they can seek security bonds,¹³ more frequent payments or monitor the taxpaying company more closely if they know of the heightened risk.

Not all company failures are followed by the resurrection of the business through a new corporate entity by the former controllers but phoenix activity seems to be particularly vexing for the creditors of the failed company. Not being paid where the company controllers are sent to the dole queue, unable to hurt others, is bad enough; to see those individuals apparently thriving in another entity, literally days after the first has folded, is infuriating. In 2012, the Inquiry into Construction Industry Insolvency in New South Wales, chaired by Bruce Collins QC, noted the frustration and anger of those affected by phoenixing by “unscrupulous operators”.¹⁴ It stated:¹⁵

Not only could the worst offenders in the industry simply close up shop one day, leaving any number and amount of debts unpaid, and opening up the next day under a different trading name, these were the same operators who were gaining an unfair competitive advantage by undercutting their rivals in the bid process.

The adverse effect on competitors was also recognised in the recent 2015 Senate Economics References Committee report into insolvency in the construction industry. It quoted a submission saying that:¹⁶

phoenix companies were “frequently winning jobs by tendering at artificially low prices made possible by the competitive advantage they receive by not complying with tax, debt and other obligations” ...

⁸ Details of the regulators involved and the provisions available to them are contained in H Anderson, A O’Connell, I Ramsay, M Welsh and H Withers, *Defining and Profiling Phoenix Activity* (Centre for Corporate Law and Securities Regulation, 2014).

⁹ *Corporations Act 2001* (Cth) s 516.

¹⁰ *Corporations Act 2001* (Cth) s 556.

¹¹ See, eg, the losses suffered by building subcontractors outlined in recent examinations of the construction industry: Australian Government, *Royal Commission into the Building and Construction Industry: Final Report Vol 8* (2003); New South Wales Government, *Final Report of the Independent Inquiry into Construction Industry Insolvency in NSW* (2012); Senate Economics References Committee, *I Just Want to be Paid: Insolvency in the Australian Construction Industry* (2015).

¹² The plight of employees is considered in H Anderson, *The Protection of Employee Entitlements in Insolvency: An Australian Perspective* (MUP, 2014).

¹³ The ATO may require a security bond for a tax-related liability under Div 255 of the *Taxation Administration Act 1953* (Cth).

¹⁴ New South Wales Government, n 11, 33, cited in Senate Economics References Committee, n 11, [5.49].

¹⁵ New South Wales Government, n 11, 33.

¹⁶ Senate Economics References Committee, n 11, [5.42].

“In such circumstances, reputable companies are simply not able to compete on price, and despite the unconscionable conduct of phoenix company operators, clients can be enticed to simply transfer the contract to the new company in order to take advantage of the lower costs on offer.”

There is no section which expressly proscribes phoenix activity, nor is there even a generally accepted definition of it. For example, the Victorian Law Reform Committee (VLRC) in 1994¹⁷ did not seek to define the activity, but rather described it as follows:¹⁸

A limited liability company fails, unable to pay its debts to creditors, employees and the State. At the same time, or soon afterwards, the same business arises from the ashes with the same directors, under the guise of a new limited liability company, but disclaiming any responsibility for the debts of the previous company.

In 1996, the Australian Securities Commission (ASC), the precursor to ASIC, produced a research paper into phoenix activity and insolvent trading. The research paper drew on a literature review, telephone survey, and in-depth interviews with community leaders and ASC staff.¹⁹ It clarified and amended the VLRC definition discussed above, pointing out several additional elements or indicators of illegal phoenixing, including the fact that:²⁰

in some instances, some creditors are paid but others are not (depending on their likelihood of taking debt recovery action); ... timeframes are difficult to specify; ... [and] the same directors or managers may not always be involved in the new business because their families or other related parties may assume those roles.

According to the 1996 ASC Research Paper, a definition of phoenix activity must include “an element of intent which separates out those who make Phoenix activities a career from those who accidentally fall foul of the ... definition through ignorance of the law and its requirements”.²¹ The paper preferred to define a phoenix company as one which “acts in a manner which intentionally denies unsecured creditors equal access to the entity’s assets in order to meet unpaid debts; and within 12 months another business commences which may use some or all of the assets of the former business, and is controlled by parties related to either the management or directors of the previous entity.”²²

While the Royal Commission into the Building and Construction Industry, known as the Cole Royal Commission, adopted the ASC definition of phoenix activity without criticism,²³ the Parliamentary Joint Committee on Corporations and Financial Services report into corporate insolvency laws noted that it was “almost impossible to define fraudulent phoenix company activity with any precision”.²⁴ Later reports have preferred a descriptive approach. The use of successor companies (one after the other) was described as “basic” phoenix activity in Treasury’s 2009 phoenix activity proposals paper.²⁵ In addition, Treasury named phoenix arrangements within corporate groups as “sophisticated” phoenix activity.²⁶

Proscribing phoenix activity based on one of the definitions above – in other words, on the outward manifestations of the behaviour – may over-regulate business rescue because it fails to take

¹⁷ Parliament of Victoria Law Reform Committee, *Curbing the Phoenix Company – First Report on the Law Relating to Directors and Managers of Insolvent Corporations*, Report No 83 (1994) <<http://www.parliament.vic.gov.au/papers/govpub/VPARL1992-94No83.pdf>>.

¹⁸ Parliament of Victoria Law Reform Committee, n 17, [1.1].

¹⁹ Australian Securities Commission, “Project One: Phoenix Activity and Insolvent Trading Public Version” (Research Paper 95/01, 1996) 11.

²⁰ Australian Securities Commission, n 19, 35–8.

²¹ Australian Securities Commission, n 19, 39–40.

²² Australian Securities Commission, n 19, 39.

²³ Australian Government, n 11, 113–14.

²⁴ Parliamentary Joint Committee on Corporations and Financial Services, *Corporate Insolvency Laws: A Stocktake* (2004) 131 [8.2].

²⁵ Treasury (Cth), “Action against Fraudulent Phoenix Activity” (Phoenix Proposals Paper, 2009) 2.

²⁶ Treasury, n 25, 2.

into account whether this is the first or 21st instance of this business being resurrected through a new corporate entity. An approach based on circumstances of the particular failed company and of its controllers has the capacity to differentiate the saving of a business with the potential to succeed from the repeated resurrection of a fundamentally flawed enterprise by incompetent controllers.²⁷ This differentiated approach would require legislative change to incorporation procedures but above all, it depends upon ASIC being in possession of comprehensive and accurate information.

Likewise, prohibiting the use of a similar name by the new company has the potential to hinder legitimate business rescues that hope to capitalise on the remaining goodwill but would allow more covert arrangements to escape notice. In 2012, the Gillard Labor government released for public comment the *Corporations Amendment (Similar Names) Bill 2012* which was part of its fulfilment of a 2010 pre-election commitment.²⁸ However, following widespread criticism, the Bill was not introduced into federal parliament.²⁹

Because of the difficulties outlined above, in order to make phoenix activity illegal, laws must proscribe the improper behaviour of the company controller – for example, the undervalued transfer of assets – rather than the fact that this undervalue occurred during a business “rescue”. Illegal phoenix activity only occurs where the controllers have, for example, breached their duties as directors to the failed company or have committed fraud.³⁰ However, discovering these breaches of duty or fraud is not easy, which hinders enforcement where that enforcement is aimed at the controllers’ improper behaviour. The problems for creditors, revenue authorities and competitors are caused not just by those breaking the law but also by those who are causing repeated losses through multiple failed attempts at running businesses. While a number of regulators have measures at their disposal that address failure to pay debts, including in the phoenix context, without requiring proof of breach of duty or fraud,³¹ even this behaviour may be hard to uncover. How these enforcement measures may be assisted by better sharing of information is discussed further in “Sharing data amongst regulators” below.

In dealing with either situation, *ex post* legal action has inevitable limitations. It is costly and inevitably involves many “offenders” escaping any consequences even where their behaviour has been uncovered. For example, upon receiving intelligence about a possible breach, ASIC³² conducts a detailed assessment of a matter when determining whether to take an enforcement action,³³ then decides whether to hold a formal investigation, following which further policy considerations come

²⁷ This is differentiated into “legal” and “problematic” phoenix activity in Anderson, O’Connell, Ramsay, Welsh and Withers, n 8.

²⁸ Australian Labor Party, “Protecting Workers’ Entitlements Package” (ALP Website, 25 July 2010) <[²⁹ For a discussion of the terms of this Bill and its fate, see H Anderson, “The Proposed Treatment of Phoenix Activity – An Opportunity Lost?” \(2012\) 34 *Sydney Law Review* 411.](http://parlinfo.aph.gov.au/parlInfo/download/library/partypol/NQGX6/upload_binary/nqgx60.pdf;fileType=application%2Fpdf#search=%22securing%20super%22>http://parlinfo.aph.gov.au/parlInfo/download/library/partypol/NQGX6/upload_binary/nqgx60.pdf;fileType=application%2Fpdf#search=%22securing%20super%22>>.</p></div><div data-bbox=)

³⁰ Relevant laws include *Corporations Act 2001* (Cth) ss 180 – 183, 588G (directors’ and officers’ duties), ss 590, 592, 596 (frauds); *Taxation Administration Act 1953* (Cth): ss 8K, 8L, 8T, 8U (tax frauds); *Criminal Code Act 1995* (Cth) s 134.2 (theft offences).

³¹ These include director penalty notices under *Taxation Administration Act 1953* (Cth) Sch 1 Div 269; and accessory liability under *Fair Work Act 2009* (Cth) s 550.

³² Australian Securities and Investments Commission, *ASIC’s Approach to Enforcement*, Information Sheet 151 (September 2013) 2, Figure 1.

³³ “What is the extent of harm or loss? What are the benefits of pursuing the misconduct, relative to the expense? How do other issues, like the type and seriousness of the misconduct and the evidence available, affect the matter? Is there an alternative course of action?”: ASIC, n 32, 2.

into play.³⁴ The ATO and the FWO also have their own litigation and debt collection policies which constrain the circumstances under which enforcement action will be launched.³⁵

Regulators are not the only parties who can bring *ex post* legal action against those involved in phoenix activity. Liquidators are empowered to finalise the affairs of the company, initiate recovery action where appropriate and to distribute those assets to creditors.³⁶ However, a lack of resources is particularly an issue for liquidators dealing with a company where its assets have been sold at an undervalue to a successor company. The more information that liquidators can access, the better the chance that properly targeted recovery action can be commenced for the benefit of creditors and the more likely it is that the liquidator can make a well-informed recommendation to ASIC as to whether this liquidation warrants further investigation. This point is considered further in “Making data available to liquidators, superannuation funds and the public” below.

Prevention or disruption of the incorporation of companies doomed to failure would go some way towards overcoming the limitations in bringing *ex post* actions against those engaging in illegal phoenix activity or those who are inept serial entrepreneurs. Potential creditors, armed with free, timely, easily obtained and accurate information might protect themselves against unwittingly entering into a transaction with a company unlikely to pay its debts. Banks might refuse them credit or seek security. The ATO might seek a security bond from someone with a string of failed companies behind them. ASIC might bring action to disqualify the person from acting as a director in future.

Creditor self-protection and the fact that there is more chance of discovery of illegal or ill-advised behaviour reduces the temptation towards opportunistic phoenix activity. The transparency measures outlined in “Gathering data” to “Making data available to liquidators, superannuation funds and the public” below have the benefit of addressing both those with the responsibility for enforcement or recovery after phoenix activity has occurred, as well as those who seek to act beforehand.

GATHERING DATA

As “Background” showed, given the enormity of phoenix activity and the flaws in current means to tackle it, a different or additional approach appears to be required. Information is the key.³⁷ It facilitates estimating the size of the problem and knowing whether most losses are caused by illegal phoenix activity or inept serial entrepreneurs. This is vital for those seeking to design effective law reform.³⁸ It also assists ASIC in locating and monitoring those individuals against whom enforcement action might be taken.³⁹ Collecting significant and verified facts about prospective company directors and their previous corporate history at the time of incorporation is the start.

³⁴ “What is the nature and seriousness of the misconduct? What was the post-misconduct behaviour of the offender? What is the strength of the case? What impact will the remedy have on: the person or entity? the regulated population? the public? Are there any mitigating factors?”: ASIC, n 32, 2.

³⁵ Fair Work Ombudsman, “Litigation” (2015) <<http://www.fairwork.gov.au/about-us/our-role/enforcing-the-legislation/litigation>>; Australian Taxation Office, “Practice Statement Law Administration”, PS LA 2011/14: General debt collection powers and principles, <<http://law.ato.gov.au/atolaw/view.htm?Docid=PSR/PS201114/NAT/ATO/00001>>.

³⁶ *Corporations Act 2001* (Cth) s 477(2).

³⁷ For example, the SERC noted that “information is critical in inhibiting illegal phoenix activity and in preventing small-scale insolvencies turning into larger collapses”: Senate Economics References Committee, n 11, [12.15].

³⁸ See Senate Economics References Committee, n 11, [2.16]: “In order to ascertain and determine appropriate responses to insolvency in the construction industry, an accurate record documenting all incidents of insolvencies is required. Unfortunately, some submissions noted that corporate insolvency statistics are inadequate at present. This is an enduring complaint for many in the industry.” (footnotes omitted).

³⁹ Productivity Commission, *Business Set-up, Transfer and Closure Final Report* (2015) 425: “The Commission considers that rather than crafting new offences, improvements in the detection and enforcement of existing laws are likely to be the best option for creating a genuine disincentive for directors contemplating phoenix action.”

Director identity number

At present, the registration of an Australian company simply requires the name, address, and date and place of birth of each proposed officeholder.⁴⁰ ASIC's form⁴¹ does not ask for the prior corporate history of its proposed directors. No supporting evidence about the identity of the proposed directors is required and ASIC does not independently verify the information provided. This allows for the possibility of fictitious directors being named, for "errors" such as the incorrect date of birth being recorded, and for versions of names, including abbreviations or maiden names, to be used. Each of these possibilities makes ASIC's detection and enforcement role more difficult. The first step in overcoming these deficiencies would involve requiring the proposed director of a company to establish their own identity. Requiring would-be directors to establish their identity via 100 points of identity proof would accord with the well-accepted and uncontroversial practice of opening bank accounts and obtaining passports. Lenders and credit ratings agencies would be further beneficiaries of a proper identification system.

The introduction of a director identity number (DIN), following the independent establishment of a person's identity, would allow regulators to track directors who engage in phoenix activity – both illegally or as inept serial entrepreneurs – more effectively. Requiring people to cite their DIN upon the incorporation of a company would assist ASIC in "joining the dots" between multiple failed companies so that they might seek to have a person with a consistent history of insolvent companies banned from managing any further companies. This could be done by ASIC as an exercise of its administrative power under s 206F or ASIC could seek a court order under s 206D. It would assist ASIC in discovering if disqualified persons attempt to register as directors. It would also allow regulators to know that Frank Nadinic, Frane Nadinic and Frank Nadimic are the same person.⁴² Currently, regulators do not necessarily connect each of these people, and insolvency practitioners and others have to conduct separate searches for each variant of a name. This is a waste of time and money for all concerned.

The regulator's suspicions might be raised when a person's DIN is used for the directorships of dozens of companies that the person could not possibly be managing or supervising in compliance with their legal obligations.⁴³ Anecdotally, we hear that pensioners are sometimes paid a fee to be nominated as a company director, in order to shield a person not wanting to come to ASIC's attention. The DIN could be used as part of a computer-based algorithm that identifies unusual patterns in data. This sort of identification, done solely based on names and dates of birth and their variants, is expensive and extremely time-consuming. Moreover, a DIN would also assist the ATO in data gathering. The ATO's extensive database could prompt its phoenix risk team to investigate instances where an elderly person with no assessable income appears to be running one or more companies. The advantages of a DIN are obvious for agencies such as the Australian Crime Commission and the Australian Federal Police, who are seeking to track those associated with organised crime⁴⁴ and complex illegal phoenix activity.

⁴⁰ *Corporations Act 2001* (Cth) s 117(2).

⁴¹ ASIC Form 201, "Application for registration as an Australian company".

⁴² This true example was cited in Senate Economics References Committee, n 11, [12.31]. Mr Nadinic acknowledged registering 32–33 companies under these names.

⁴³ For example, their duties as directors under *Corporations Act 2001* (Cth) Pt 2D.1.

⁴⁴ See, eg, Australian Crime Commission, *Organised Crime in Australia 2015* (ACC, 2015) 8, 25–6, 65–6.

The recommendation of a DIN⁴⁵ was made to the Productivity Commission in response to a December 2014 issues paper⁴⁶ considering business set up, transfer and closure.⁴⁷ Its draft report in May 2015 agreed with the proposal, noting that it:⁴⁸

considers that the benefits of tracking through data matching for regulators should outweigh the relatively low compliance costs for directors. Concerns about privacy can also be overcome in a manner similar to other confidential data held by agencies such as the ATO. To reduce compliance costs, DINS should be available online at the time of an individual's first directorship.

In its final report released in December 2015, the Productivity Commission recommended adoption of the DIN both for new and existing directors,⁴⁹ noting broad support for the concept, even from directors themselves.⁵⁰ It recommended that the history of the DIN would be publicly available,⁵¹ so that a person could see that a director whose company they were proposing to do business with – Fred Nerks, DIN 123 456 789, director of Acme Pty Ltd – had in fact been associated with 20 previously failed companies. The usefulness of the DIN by the public, to be addressed further in “Making data available to liquidators, superannuation funds and the public” below, therefore depends upon companies being required to state their directors' names and DINs in their dealings with prospective clients, whether those dealings are conducted by the directors themselves or by the company's employees. For example, quotes, contracts and invoices could display this information, or the company's paperwork could clearly direct people towards a website that contained this information, required to be kept current. The latter suggestion would overcome any objection that each change of director would necessitate the production of new corporate stationery.

One significant issue with the DIN is the Productivity Commission's comment that “the identity check could be completed online”.⁵² This response to concerns about compliance costs to both business and ASIC may be misguided, as there is greater scope for fraud where documents are scanned and uploaded, rather than viewed in person. While applications for passports, bank accounts and drivers licences may be initiated online, the identity proof for each must be provided later via original documents produced by the applicant. The 2015 Senate Economics Reference Committee (SERC) Construction Insolvency Report recognised the importance of independent verification “to ensure that information provided to ASIC when an individual becomes a company director is accurate. As the collector of company information, the committee believes that ASIC should be required to verify it.”⁵³

⁴⁵ “The benefits, in terms of even a small reduction in illegal phoenix activity are potentially quite large”: Australian Securities and Investments Commission, *Productivity Inquiry into Business Set Up, Transfer and Closure: ASIC's Supplementary Submission DR58* (2015) 15. Further, the use of DINs should make tracking directors simpler for administrators and liquidators, reducing the time and thus cost of insolvency processes. Therefore, the Commission is confident that the introduction of a DIN is likely to be of significant net benefit to the community as a whole. Indeed, as the Australian Business Register (Submission DR51) submitted, the DIN could be used to link with other existing databases, to identify those businesses involving directors with a history of repeated insolvencies. This information could be used for “early intervention” either in compliance and enforcement or in providing targeted assistance (particularly education of responsibilities). See also Productivity Commission, n 39, 425.

⁴⁶ H Anderson, I Ramsay, A O'Connell and M Welsh, *Submission No 1 to Australian Government, Productivity Commission, Business Set-up, Transfer and Closure Issues Paper* (December 2014).

⁴⁷ Anderson, Ramsay, O'Connell and Welsh, n 46. The suggestion of a DIN was also made in 2013: H Anderson, “An Ounce of Prevention: Practical Ways to Hinder Phoenix Activity” (2013) 25 *Australian Insolvency Journal* 16.

⁴⁸ Productivity Commission, *Business Set-up, Transfer and Closure Draft Report* (May 2015) 383.

⁴⁹ Productivity Commission, n 39, recommendation 15.6. Note that the Productivity Commission also endorsed the DIN in its report: Productivity Commission, *Workplace Relations Framework Inquiry Report* (December 2015) Vol 1, 48; Vol 2, 915, 938, <<http://www.pc.gov.au/inquiries/completed/workplace-relations/report>>.

⁵⁰ Productivity Commission, n 39, 426.

⁵¹ Productivity Commission, n 39, 427.

⁵² Productivity Commission, n 39, 427.

⁵³ Senate Economics References Committee, n 11, [12.35].

A cost-saving solution noted by the Productivity Commission is that “the DIN could be instituted as a marginal addition onto other regulatory requirements (for example in relation to Australian Business Numbers).⁵⁴ A business’s Australian Business Number (ABN) must appear on its invoices and other stationery. Application for an ABN requires the applicant to produce a tax file number (TFN) or alternatively prove their identity.⁵⁵ The TFN itself requires the completion of a form – online – and then a subsequent identity check at a post office or other prescribed location.⁵⁶ For the TFN to act as a de facto DIN, the *Income Tax Assessment Act 1936* (Cth) would need to be amended to require company directors to hold a TFN⁵⁷ and the *Corporations Act 2001* (Cth) would need to be amended to require company directors to quote their TFN on the application to incorporate a company.⁵⁸ To maintain consistency with the TFN regime, it could be possible to opt out of obtaining a DIN or disclosing it to selected parties, at the cost, perhaps, of being required to lodge a bond with ASIC and the ATO. This is analogous to being required to remit the top rate of tax where no TFN is quoted.⁵⁹

At present, searching the Australian Business Register (ABR) does nothing to assist the public in their own self-protection. Upon entering a company’s name, ABN Lookup⁶⁰ shows the company’s ABN status (eg active), the entity type (eg Australian private company), its GST registration status, its location by postcode and its eligibility to receive tax deductible gifts. It also directs the searcher to the company’s ASIC Connect record, which in turn reveals the company’s ACN and date of company registration. ASIC Connect also offers various other documents about the company for sale,⁶¹ although none of these documents relate to the prior corporate history of the directors or officers. In other words, the present searching mechanisms offer very little meaningful information for those to learn about the propensity of certain company controllers towards phoenix activity.

It is important to recognise that neither a direct DIN requirement nor the TFN indirect approach would address changes of directorship or control of the company once it is already established. In particular, there are two alternative scenarios that are problematic here. The first is where the real controller is registered as director of a company upon its incorporation but once the company fails and if ASIC investigates, a back-dated “change of directorship” form⁶² is lodged which lists a “straw man” as the director at the time of any infraction.⁶³ The second is where an innocuous person, perhaps a relative, is named as the director at the time of the incorporation but a fraudster or inept serial entrepreneur assumes actual control of the company. While this innocuous person runs the small risk

⁵⁴ Productivity Commission, n 39, 427.

⁵⁵ See <https://abr.gov.au/For-Business,-Super-funds---Charities/Applying-for-an-ABN/What-you-need-for-your-ABN-application/TFN>.

⁵⁶ See <https://www.ato.gov.au/individuals/tax-file-number/apply-for-a-tfn/australian-residents---tfn-application>.

⁵⁷ *Income Tax Assessment Act 1936* (Cth) s 202. Sections 8WA and 8WB of the *Taxation Administration Act 1953* (Cth) make it an offence to require or request that a TFN be quoted or to record, use or disclose a TFN, other than in specified circumstances. The incorporation of a company would need to be added to that list of specified circumstances.

⁵⁸ *Corporations Act 2001* (Cth) s 117.

⁵⁹ See further <https://www.ato.gov.au/Rates/Fortnightly-tax-table/?page=2>.

⁶⁰ See <http://abr.business.gov.au>.

⁶¹ Under s 4 of the *Corporations (Fees) Act 2001* (Cth), a “chargeable matter” includes “(c) the inspection or search of a register kept by, or a document in the custody of, ASIC ...” and “(d) the making available by ASIC ... of information (whether in the form of a document or otherwise)”.

⁶² *Corporations Act 2001* (Cth) Form 484.

⁶³ While the official requirement is that dated forms must be lodged within 28 days, ASIC accepts late forms provided a fee is paid: <http://asic.gov.au/for-business/changes-to-your-company>. The Australian Business Register, on the other hand, requires changes to prescribed information, including the names and addresses of representatives and associates of ABN holding entities, to be notified within 28 days. According to *A New Tax System (Australian Business Number) Act 1999* (Cth) s 14, failure to do so is an offence under s 8C of the *Taxation Administration Act 1953* (Cth).

of being held to account if the company fails, creditors are deprived of the *ex ante* protection that greater transparency is intended to provide. As the Productivity Commission noted, the DIN is not a “magic bullet”.⁶⁴

The three objectives of the DIN are to deter those seeking to improperly use the corporate form to avoid payment of accruing debts, to allow creditor self-protection against phoenix activity, and where that behaviour still occurs, to enable regulators to more easily enforce laws against the wrongdoers.⁶⁵ Given the broad support that the proposal has received to date, it might appear inevitable that it be adopted. Countries as diverse as India⁶⁶ and Estonia⁶⁷ have director verification procedures, and the DIN is part of the platform of the Australian Restructuring Insolvency and Turnaround Association (ARITA). It was also supported by the Senate Economics References Committee’s inquiry into insolvency in the construction industry.⁶⁸ However, as is discussed further below, as yet there is no response from government about the DIN recommendation.⁶⁹

Company registration

As an adjunct to the DIN, the company registration process could also be improved to provide significantly more information to ASIC. There are presently two ways to incorporate a company. The first is to purchase one already incorporated by a business service provider that has an online link to ASIC. Alternatively, a paper form can be completed and mailed to ASIC by the prospective director.⁷⁰ In either case, ASIC lacks the capacity to adapt the registration process to address any responses to the questions on the form. To overcome this without inhibiting legitimate business activity, it is suggested that the form should be completed online by the prospective director themselves and that the incorporation and purchase of shelf companies from business service providers be stopped. It is surely not unreasonable to expect a business person to possess the computing capabilities and intellectual ability to complete such a form upon incorporating a company. Where directorships change after the company is established, these questions could be asked on the “change of company details” form.⁷¹

The online form would ask additional questions of the prospective director via drop-down menus. Having cited the director’s DIN, the form could ask whether the person has ever managed any other company. If the answer is no, then the rest of the form is simple and quick to complete. If yes, then a drop-down menu could require more information. Further questions could include whether the other companies are still in existence and if not, whether they paid their creditors in full or less than 50 cents in the dollar. Again, answers indicating a poor track record could prompt more questions. It is fair that a person who wants another opportunity to run a company should provide this level of detail. The aim here is to equip ASIC with information about this person, allowing the regulator to take appropriate action which may include placing them on a watch list. A secondary but equally important aim is to alert the would-be director to the fact that *ASIC knows this information*, thereby

⁶⁴ Productivity Commission, n 39, 427.

⁶⁵ The senate inquiry noted that “[t]he inability of regulators and participants in the building and construction industry to identify and track individuals suspected of illegal activity is a significant cause of the incidence of illegal phoenix activity”: Senate Economics References Committee, n 11, xxvi.

⁶⁶ See further <<http://www.mca.gov.in/MCA21/dca/din/DIN.html>>.

⁶⁷ Estonia offers corporate e-residency which is a form of digital identification. It requires directors to provide identity card information which has already verified the person’s identity. See further <<https://e-estonia.com/e-residents/about>>.

⁶⁸ Senate Economics References Committee, n 11, recommendations 36 (DIN) and 37 (proof of identity). Recommendation 38 called on the *Australian Securities and Investments Act 2001* (Cth) to be amended to require ASIC to verify company information.

⁶⁹ Note that the DIN proposal is not to be confused with the Coalition government’s “streamlining business registration” initiative, <<http://www.business.gov.au/for-government/Pages/Streamlining-business-registration.aspx>>. It was announced under the *Growing Jobs and Small Business* package that the government would develop a single online portal for business and company registration and establish a single business identifier. The underlying requirements for various registrations would not change; rather, a single portal would accommodate multiple registrations, such as for business names, GST or FBT.

⁷⁰ See <<http://asic.gov.au/for-business/starting-a-company/how-to-start-a-company>>.

⁷¹ *Corporations Act 2001* (Cth) Form 484.

discouraging them from engaging in illegal phoenix activity by interfering with its invisibility. If the director provides false information, ASIC may prosecute them.⁷²

Information from RATA and external administrator reporting

There are two other major sources of information that are not fully exploited by ASIC. The first is the Report as to Affairs (RATA)⁷³ that is completed by company directors at the time of the company's insolvency and given to the external administrator. At present, this form does not ask any questions about previous company failures with which this director has been associated. This is a missed opportunity to alert the liquidator to facts which might encourage further investigation and an application to the Assetless Administration Fund.⁷⁴

The second is the information provided by external administrators to ASIC at the conclusion of an administration. Greater disclosure about the circumstances of the company's failure could be required in their reporting.⁷⁵ A central part of this reporting relates to misconduct by corporate controllers before and during external administrations. Liquidators notify ASIC whether they suspect the conduct breaches civil penalty or criminal laws, and whether they hold documentary evidence to support their claims. This is vital intelligence that ASIC uses to select cases to pursue further. At present, the return submitted to ASIC requires a tick-box to indicate that breaches of duty and other civil or criminal offences are suspected. These forms should be amended to allow for comments to be made. In addition, a further tick-box could be inserted so that administrators could report that the breach occurred in a suspected phoenix context. This suggestion was expressly endorsed by the 2015 SERC Construction Insolvency Report.⁷⁶ This data would be also enormously beneficial for regulators who seek to understand the scope of the problem.

However, all of the above data-gathering suggestions need to be read in the light of the government's pro-innovation and anti-red tape push. Late in 2015, Prime Minister Turnbull and Innovation and Science Minister Christopher Pyne came out strongly⁷⁷ in favour of supporting repeated attempts at business enterprise after earlier failures.⁷⁸ The government has committed to the reduction of red tape across government, including the \$1 billion annual regulation cost reduction target.⁷⁹ Nevertheless, it is a mistake to view insolvency reporting requirements simply as costs to be minimised. They not only provide valuable information to ASIC but also make it clear to the failed companies' controllers and administrators that ASIC will be armed with the information to take action in appropriate circumstances. The compliance costs to business are minimal; indeed, competitor

⁷² *Corporations Act 2001* (Cth) s 1308(2).

⁷³ *Corporations Act 2001* (Cth) Form 507. See <<http://asic.gov.au/regulatory-resources/forms/forms-folder/507-report-as-to-affairs>>.

⁷⁴ The Assetless Administration Fund (AAF) is administered by ASIC. With funds provided by the government, it finances insolvency practitioners in their work on behalf of companies with few or no assets. The aim of the fund is to overcome the inability of liquidators to make proper investigations due to financial constraints. "A particular focus of the AAF is to curb fraudulent phoenix activity": Australian Securities and Investments Commission, *Assetless Administration Fund: Funding Criteria and Guidelines and Appendices 1 to 10*, Regulatory Guide 109 (November 2012) RG109.6.

⁷⁵ Australian Securities and Investments Commission, *External Administrators – Reporting and Lodging*, Regulatory Guide 16. The form is "EX01 Schedule B of Regulatory Guide 16 – Report to ASIC under ss 422, 438D or 533 of the *Corporations Act 2001* (Cth) or for Statistical Purposes". In December 2014, EX01 was changed to ask for additional information where insolvent trading was alleged. No amendment was made with respect to phoenix activity.

⁷⁶ Senate Economics References Committee, n 11, [5.34], recommendation 11: The committee recommends that ASIC, in consultation with ARITA, work out a method whereby external administrators can indicate clearly in their statutory reports whether they suspect phoenix activity has occurred. For example, to serve as a red flag to ASIC, include a box in the reporting form that external administrators would tick if they suspected phoenix activity.

⁷⁷ National Innovation and Science Agenda, *Welcome to the Ideas Boom* (NISA, 2015) <<http://www.innovation.gov.au/page/national-innovation-and-science-agenda-report>>.

⁷⁸ "We need a greater emphasis on celebrating success rather than penalising failure. This takes a cultural shift to encourage more Australians and businesses to take a risk on a smart idea. We need to leave behind the fear of failure, and challenge each other to be more ambitious": NISA, n 77, 6.

⁷⁹ See <<https://cuttingredtape.gov.au/annual-reports/annual-deregulation-report-2014/deregulation-savings-and-costs>>.

companies will benefit through the removal of fraudsters who unfairly gain contracts through tendering based on the non-payment of debts. The potential saving of tax revenue currently lost through phoenix activity also opens up the possibility of reducing the tax burden on compliant businesses.

SHARING DATA AMONGST REGULATORS

As “Background” noted, liquidators and ASIC are the main actors in terms of bringing enforcement or recovery action against errant company controllers engaged in phoenix activity. However, there are a range of actions that can be brought by other regulators, both before and after the phoenix activity has occurred. All of these actions are dependent on the particular regulator being provided with the necessary information. For example, the ATO can bring actions for a range of tax crimes.⁸⁰ Likewise, the FWO has the ability to seek a penalty against a director where the employer company has failed to pay wages and other entitlements.⁸¹ The ATO can also seek a security bond where there is a risk that a tax liability will not be met.⁸² Criminal offences can be prosecuted by the Australian Federal Police with respect to fraud or organised crime.⁸³

Each of these agencies is a member of the Interagency Phoenix Forum (IAPF).⁸⁴ While there is much goodwill between these regulatory agencies and a genuine commitment to the disruption of illegal phoenix activity, information does not flow freely. For example, the ATO is the host of the Australian Business Register’s Phoenix Watchlist. The ATO provides data about suspected phoenix operators to the list but it is difficult to discover whether the other IAPF members are providing similar information.⁸⁵ The IAPF is now a prescribed task force,⁸⁶ which allows the exchange of tax information within the forum.⁸⁷ However, according to the ATO, it does not permit that information to be passed on by recipient agencies to others within the forum, or for the ATO to receive information from other agencies.⁸⁸ This apparent lack of co-operation led the 2015 SERC Construction Insolvency Report to make a formal recommendation that “consideration be given to amending confidentiality

⁸⁰ See n 30.

⁸¹ *Fair Work Act 2009* (Cth) s 545 allows a court to make an order for breach of a civil remedy provision. This includes a penalty: s 546(1). Contravening a modern award or enterprise agreement are civil remedy provisions: ss 45, 50 respectively. Directors as accessories are also subject to the penalty where their involvement in the breach has been established under s 550.

⁸² *Taxation Administration Act 1953* (Cth) Sch 1, s 255-100.

⁸³ *Criminal Code Act 1995* (Cth) s 134.1 (obtaining property by deception); s 134.2 (obtaining a financial advantage by deception); s 135.4(3) (conspiracy to defraud a Commonwealth entity); s 400.3 (dealing with the proceeds of crime). See also the Serious Financial Crime Taskforce, established in July 2015, <http://www.tax-news.com/news/Australia_Launches_Serious_Financial_Crime_Taskforce_69444.html>: “Key operational priorities for the Taskforce over the first two years will include investigations into serious international tax evasion and criminality related to trusts and phoenix activity – when companies deliberately and repeatedly liquidate to avoid paying creditors, employee entitlements and taxes.”

⁸⁴ A full list of member agencies is available at <<https://www.ato.gov.au/General/The-fight-against-tax-crime/Our-focus/Fraudulent-phoenix-activities>>.

⁸⁵ In its April 2015 submission to the Senate Standing Committee on Economics inquiry into insolvency in the Australian construction industry, the ATO noted that it had “provided information regarding 154 confirmed Phoenix operator groups with 2,184 linked entities through the Phoenix Watchlist” and that it was working to provide further data in the future: Australian Taxation Office, *Submission to the Senate Economic References Committee on Insolvency in the Construction Industry* (ATO, 2015) 20. No other submissions by regulators indicated that any intelligence had been provided to the watchlist, nor is there any other publicly available information to that effect.

⁸⁶ *Taxation Administration Act 1953* (Cth) Sch 1, 355-70(12): “The regulations [*Taxation Administration Regulations 1976* (Cth)] may prescribe a taskforce for the purposes of item 4 of the table in subsection (1). A major purpose of the taskforce must be protecting the public finances of Australia.” Regulation 48 of the *Taxation Administration Regulations 1976* has the current list of prescribed taskforces: <http://www5.austlii.edu.au/au/legis/cth/consol_reg/tar1976378/s48.html>.

⁸⁷ *Taxation Administration Act 1953* (Cth) Sch 1, 355-70, table headed “Records or disclosures for law enforcement and related purposes” item 4, inserted by the *Tax Laws Amendment (Confidentiality of Taxpayer Information) Act 2010* (Cth).

⁸⁸ Senate Economics References Committee, n 11, [5.64].

requirements in statutory frameworks of agencies participating in the Phoenix Taskforce to permit dissemination of relevant information to the ATO.”⁸⁹ The Coalition Senators’ Additional Comments at the end of that report also noted that:⁹⁰

As these agencies are characterised by a diversity of aims, powers and responsibilities, any changes to the operation of the Taskforce, including the changes to confidentiality requirements outlined in Recommendation 12, would need to be considered by all the relevant agencies and would take time to resolve.

Yet the law already appears to allow exchanges of information relevant to illegal phoenix activity. For example, ASIC enjoys extensive powers of disclosure, with appropriate safeguards, under s 127 of the *Australian Securities and Investments Commission Act 2001* (Cth).⁹¹ The ATO’s powers of disclosure are outlined in the *Taxation Administration Act 1953* (Cth), where it may disclose information to a variety of other agencies including ASIC in specified circumstances.⁹² When these powers were inserted in 2010, the preceding explanatory memorandum expressly acknowledged that “[i]nformation held by the ATO may be invaluable for ASIC in pursuing action against directors who may repeatedly be engaged in fraudulent phoenix activity.”⁹³ It appears that secondary disclosure – passing on received information to a third agency – is permissible under some legislation with sufficiently senior sign-off.⁹⁴ It is possible that government agencies adopt a risk-averse approach to sharing information to avoid possible breaches of confidentiality rules.⁹⁵

With the adoption of the measures recommended in the section “Gathering data” above, the ABR could be a useful platform for information sharing by government agencies. The ABR has two portals – ABN Lookup, discussed above, which is available to the public and ABR Explorer, which is available to all eligible government agencies.⁹⁶ The latter is relevant to the present discussion. It allows specified agencies, upon agreeing to various privacy constraints, to access ABR non-public data. This includes the names and addresses of representatives and associates of ABN holders. At present, this is of limited utility because the information does not extend to the prior corporate history

⁸⁹ Senate Economics References Committee, n 11, [5.84], recommendation 12.

⁹⁰ Senate Economics References Committee, n 11, 197.

⁹¹ Pursuant to *Australian Securities and Investments Commission Act 2001* (Cth) s 127(2), “the disclosure of information as required or permitted by a law of the Commonwealth or a prescribed law of a State or internal Territory is taken to be authorised use and disclosure of the information”. In addition, s 127(4) provides that “Where the Chairperson is satisfied that particular information ... (b) will enable or assist the government, or an agency, of a State or Territory to perform a function or exercise a power; ... the disclosure of the information to the agency, government, officer or body by a person whom the Chairperson authorises for the purpose is taken to be authorised use and disclosure of the information.”

⁹² *Taxation Administration Act 1953* (Cth) Sch 1, s 355-65. According to the Explanatory Memorandum to the *Tax Laws Amendment (Confidentiality of Taxpayer Information) Bill 2010* (Cth), the aim of the Bill was to consolidate and standardise privacy provisions that had previously been spread over many pieces of legislation. While “[t]he key principle of the new framework is the protection of taxpayer information ... [d]isclosures of information are, however, permitted in instances where privacy concerns are outweighed by the public benefit of those disclosures.”

⁹³ *Tax Laws Amendment (Confidentiality of Taxpayer Information) Bill 2010* (Cth) Explanatory Memorandum, [5.55].

⁹⁴ See, eg, *Taxation Administration Act 1997* (Vic) s 94 which allows further disclosure of information obtained from a tax officer where it is for the purpose of the enforcement of the law or protecting the public revenue, where the Commissioner consents to the disclosure. The primary disclosure was permitted under s 92(1) of that Act where it was made “(e) to an authorised recipient”. What follows is a list of government agencies, as well as the “Legal Services Board and ... the Victorian Legal Services Commissioner”.

⁹⁵ See Australian Law Reform Commission, *Secrecy Laws and Open Government in Australia*, Report 112 (2009) [15.54]: “... agency culture can prevent information from being disclosed in situations where disclosure would be lawful and appropriate”. The ALRC also quoted a 2008 Independent Review Panel examining the *Freedom of Information Act 1992* (Qld): “Inherent at an organisational level, the urgency of the everyday imperatives in modern government can pull the public sector’s information culture towards information protection in the interests of issues management, at the expense of the important but less urgent information goals for transparency in government.”

⁹⁶ See <<https://abr.gov.au/For-Government-agencies/Accessing-ABR-data/ABR-Explorer>>. At present 502 agencies from federal, state and local government have access to ABR explorer.

of those people. Allowing ASIC to contribute to ABR information, and for that information to be available to other permitted agencies would significantly improve the flow of useful information amongst agencies.

For example, at present, if the FWO receives a report that Honest Trolley Hire Pty Ltd has been underpaying its workers, it can conduct an ASIC search to discover that its sole director is Joe Bloggs and can bring an accessory action against him.⁹⁷ But it cannot discover that Joe has done a similar thing with the previous 15 entities that he has controlled because it cannot search for his name on anything other than the listing of banned directors. Access to Joe's previous corporate history would allow the FWO to decide how strongly to pursue the case and whether, for example, it should proceed to court or accept an enforceable undertaking. It could also use this information in a referral to ASIC that Joe may have breached his duty as a director by deliberately liquidating companies to avoid large fines against them.

ASIC currently provides the ABR with information about companies entering external administration or being deregistered for failure to pay fees. This prompts the ABR to cancel the company's ABN. One innovation that would not require any new legislation would be for the ABR, if it discovered that the people associated with a cancelled ABN were seeking a new ABN, to alert ASIC and other agencies of this activity under the rubric of the ABR Explorer. This would not involve an implication of wrongdoing. It would simply allow agencies that might be looking at certain individuals or industries to have better knowledge about their activities.

It is time for the government to review the wider dissemination of information about possible phoenix activity. A review should reveal whether new law is needed or simply more and better attempts by regulatory agencies to use the information exchange powers that they already have. It is hoped that this occurs as part of the Productivity Commission's inquiry into data availability and its use, announced in April 2016.⁹⁸

MAKING DATA AVAILABLE TO LIQUIDATORS, SUPERANNUATION FUNDS AND THE PUBLIC

While providing information to regulators will undoubtedly assist them in bringing enforcement action against errant directors engaging in phoenix activity, whether illegally or as inept serial entrepreneurs, their resource constraints inevitably mean that liquidators, superannuation funds and the general public must take some responsibility for policing phoenix activity. As with regulators, these parties would benefit enormously from the greater availability of corporate information.

Liquidators

As explained above, liquidators provide ASIC with information about the external administration, but while this is a statutory obligation,⁹⁹ it is nonetheless a by-product of their main role. Liquidators are responsible for finalising the affairs of companies being wound up, recovering company assets including via litigation, and distributing them amongst eligible creditors.¹⁰⁰ To enable them to perform this role, it would be highly beneficial if liquidators received information *from* ASIC. Because liquidators have professional obligations of independence,¹⁰¹ they are not familiar with the prior corporate history of the directors who engage them to wind up their insolvent companies. At present,

⁹⁷ See n 81.

⁹⁸ Productivity Commission, *Data Availability and Use*, Issues Paper (2016). Its terms of reference, at iv – v, are broad enough to encompass the matters raised above.

⁹⁹ See *Corporations Act 2001* (Cth) s 545: "(1) Subject to this section, a liquidator is not liable to incur any expense in relation to the winding up of a company unless there is sufficient available property. ... (3) Nothing in this section is taken to relieve a liquidator of any obligation to lodge a document (including a report) with ASIC under any provision of this Act by reason only that he or she would be required to incur expense in order to perform that obligation."

¹⁰⁰ *Corporations Act 2001* (Cth) s 477.

¹⁰¹ Australian Restructuring Insolvency and Turnaround Association, *Code of Professional Practice* (3rd ed, ARITA, 2014) Ch 6.

liquidators are required to seek this information from publicly available registers for a fee.¹⁰² The fee charged does not need to bear any relationship to the cost of providing the service.¹⁰³

This is particularly problematic in the phoenix context. Since the usual aim of illegal phoenix activity is to ensure that creditors are not paid what they are entitled to, liquidations of phoenixed companies commonly have few or no assets. Illegal phoenixing succeeds because the very act of stripping assets from the liquidated company deprives the liquidator of the means to be paid for making a proper investigation. There is no obligation to conduct any investigations beyond the bare minimum required for the statutory report.¹⁰⁴ This means that liquidators are expected to conduct investigations and seek information *from* ASIC, to report *to* ASIC, but do so at their own expense. It would seem indisputable that more could be done by liquidators in delving into suspect corporate transactions if they did not have to incur these expenses.

Superannuation funds

When a company enters liquidation, employees with unpaid entitlements are entitled to claim on the taxpayer-funded Fair Entitlements Guarantee (FEG),¹⁰⁵ which covers specified amounts of wages, leave and redundancy entitlements. However, superannuation is not covered by FEG.¹⁰⁶

Superannuation recovery is subject to a peculiar mechanism. The employer is obliged to pay at least the statutory mandated amount¹⁰⁷ to the employee's chosen fund¹⁰⁸ but the fund is not, strictly speaking, a creditor in the winding up.¹⁰⁹ In practice, the fund might chase the employer for the payment but is obliged to be satisfied with the employer's answer. The employer might reply that the employee has changed funds or is no longer employed there. The enforcement of superannuation comes through the superannuation guarantee charge which is administered by the ATO,¹¹⁰ but the ATO relies on the employer to self-declare their failure to pay.¹¹¹ An ATO investigation may be prompted by employee complaints¹¹² that superannuation has not been paid but for a variety of reasons, the ATO may not initiate recovery action or may be unable to recover the outstanding amount.¹¹³ The employee may be unaware of the non-payment until the employer company becomes insolvent.¹¹⁴

Because of the multiple parties involved in superannuation – employee, employer, trade union, superannuation fund, ATO – information is vital to ensure that unremitted payments are followed up as soon as possible. This was recognised by the 2015 SERC Construction Insolvency Report which

¹⁰² Under s 4(1) of the *Corporations (Fees) Act 2001* (Cth), “chargeable matter” includes “(c) the inspection or search of a register kept by, or a document in the custody of, ASIC ...” and “(d) the making available by ASIC ... of information (whether in the form of a document or otherwise)”.

¹⁰³ *Corporations (Fees) Act 2001* (Cth) s 6(2).

¹⁰⁴ *Corporations Act 2001* (Cth) s 545: “(1) Subject to this section, a liquidator is not liable to incur any expense in relation to the winding up of a company unless there is sufficient available property. ... (3) Nothing in this section is taken to relieve a liquidator of any obligation to lodge a document (including a report) with ASIC under any provision of this Act by reason only that he or she would be required to incur expense in order to perform that obligation.”

¹⁰⁵ See <<https://www.employment.gov.au/fair-entitlements-guarantee-feg>>.

¹⁰⁶ Under *Fair Entitlements Guarantee Act 2012* (Cth) s 5, an “employment entitlement” under the Act means annual leave, long service leave, payment in lieu of notice, redundancy and wages.

¹⁰⁷ This amount is currently 9.5 per cent of eligible wages.

¹⁰⁸ *Superannuation Legislation Amendment (Choice of Superannuation Funds) Act 2004* (Cth) which inserted *Superannuation Guarantee (Administration) Act 1992* (Cth) Pt 3A.

¹⁰⁹ Employees are priority creditors under a liquidation: (see *Corporations Act 2001* (Cth) s 556(1)(e) – (h)) and superannuation is one of the entitlements which are subject to this priority.

¹¹⁰ *Superannuation Guarantee Charge Act 1992* (Cth); *Superannuation Guarantee (Administration) Act 1992* (Cth) s 64A.

¹¹¹ *Superannuation Guarantee (Administration) Act 1992* (Cth) s 46.

¹¹² See <<https://www.ato.gov.au/Individuals/Super/In-detail/Growing/Unpaid-super/?page=4>>.

¹¹³ See <<https://www.ato.gov.au/Individuals/Super/In-detail/Growing/Unpaid-super>>.

¹¹⁴ See further H Anderson and T Hardy, “Who Should be the Super Police? Recovery of Unremitted Superannuation in Insolvency” (2014) 37 *University of New South Wales Law Journal* 162.

recommended better liaison between the ATO, ASIC and superannuation funds to assist early detection,¹¹⁵ and that privacy provisions be reviewed to facilitate improved information sharing.¹¹⁶ While some liaison and information sharing is already taking place, the superannuation fund for the building industry, Cbus, submitted to the SERC that “resourcing limitations continue to curtail the proactive work that the ATO can undertake”.¹¹⁷ This may have contributed to employees of Cbus giving fund-member information to the fund-members’ union, the CFMEU. This improper action was brought to light in 2015 by the Royal Commission into Trade Union Governance and Corruption (Heydon Royal Commission) in relation to non-payments of superannuation by a company called Lis-Con.¹¹⁸

The public as creditors

As noted above, employees are company creditors but they enjoy the benefits of FEG as well as their status as priority creditors in a liquidation. In terms of information about insolvency, they are more likely to be aware of the company’s precarious financial position, for example through reduced orders or late wage payments, even if they are unable to act on that information effectively.¹¹⁹

The parties who lack access to information but for whom information is crucial for self-protection are independent contractors and other unsecured trade creditors. Because these parties are unable to enforce their debts directly once the company enters liquidation,¹²⁰ any recovery they receive is at the lowest rank of unsecured creditor. This typically is less than 11 cents in the dollar.¹²¹ These parties need information *before* any contract is entered into¹²² so that a decision can be made whether to do business with this company at all and if so, what price to charge. Once again, this lack of information was highlighted by the 2015 SERC Construction Insolvency Report, and their first recommendation was that:¹²³

ASIC conduct a review of administrators’ and liquidators’ reporting requirements and the range and extent of information it requires to be reported and, where necessary, make changes that will ensure the regulator is able to fully inform itself, the Parliament and the public with complete, relevant and up-to-date data on insolvencies.

¹¹⁵ Senate Economics References Committee, n 11, [3.72], recommendation 5: “The committee recommends that the ATO and ASIC increase their formal cooperation with superannuation funds to coordinate measures around early detection of non-payment of superannuation guarantee.”

¹¹⁶ Senate Economics References Committee, n 11, [3.73], recommendation 6: “The committee recommends that privacy provisions which may inhibit information flows between the ATO and APRA regulated superannuation funds be reviewed and that the ATO seek advice from the Office of the Australian Information Commissioner as to the extent to which protection of public revenue exemptions in the Australian Privacy Principles might facilitate improved information sharing.”

¹¹⁷ Senate Economics References Committee, n 11, [3.27].

¹¹⁸ “Submissions of Counsel Assisting – Cbus Leak to the CFMEU”, <<https://www.tradeunionroyalcommission.gov.au/Submissions/Documents/2015-Submissions/CBus-Submissions/Cbus-Counsel-Assisting-Submissions.pdf>>.

¹¹⁹ For example, the employee may be unable to find alternative employment. Employees cannot require employers to pay out long service leave, redundancy or payment in lieu of notice entitlements until they accrue. Employees also do not have standing to enforce the superannuation guarantee charge to force their employer to make the statutory contributions to their nominated fund.

¹²⁰ *Corporations Act 2001* (Cth) s 471B.

¹²¹ According to Australian Securities and Investments Commission, *Report 456 Insolvency Statistics: External Administrators’ Reports (July 2014 to June 2015)* (2015), 7: “In 97% of cases, the dividend estimate was less than 11 cents in the dollar”. This was also the case in 2012–13 and 2013–14.

¹²² ASIC does allow interested parties to register under their Company Alert system, which sends a message when a specified company lodges various documents, including those relating to changes of director and external administration. See <<http://asic.gov.au/online-services/alerts>>. However, the person seeking the information must still pay to obtain the document. In addition, the alert expires annually unless renewed.

¹²³ Senate Economics References Committee, n 11, [2.62], recommendation 1.

This was followed up with recommendations about “early warning to industry participants about repeat and concerning insolvent practices”¹²⁴ and “that regulators increase engagement efforts with industry participants aimed at increasing and enhancing information flows.”¹²⁵ Of particular importance is their recommendation “that ASIC and Australian Financial Security Authority company records be available online without payment of a fee”.¹²⁶ Increased transparency in Australia would follow the trend set in European Union countries.¹²⁷ The United Kingdom announced in June 2015 that “over 170 million digital records on companies and directors including financial accounts, company filings and details on directors and secretaries throughout the life of the company” held by the UK register of companies would be searchable, free of charge.¹²⁸ According to UK Business Secretary the Hon Dr Vince Cable:¹²⁹

[t]he government firmly believes that the best way to maximise the value to the UK economy of the information which Companies House holds, is for it to be available as open data. By making its data freely available and free of charge, Companies House is making the UK a more transparent, efficient and effective place to do business.

Any initiatives to publicise information about company directors must also comply with, or be exempted from, the provisions of the *Privacy Act 1988* (Cth) which was amended in 2012.¹³⁰ The Act only covers the information of individuals, not companies, and as far as the individuals are concerned, identity verification is not covered by the *Privacy Act 1988*.¹³¹ The Australian Privacy Principles, which form part of the Act,¹³² do allow an outside organisation to adopt a government related identifier of an individual as its own identifier if it is authorised by law or regulations.¹³³

Information about prior corporate histories of directors would be covered by the *Privacy Act 1988* and must comply with both the Australian Privacy Principles and the credit reporting provisions¹³⁴ of the Act if that information were publicly disseminated by credit rating agencies. Credit managers in particular would like to see information about prior tax defaults by companies who are seeking credit.¹³⁵ At present, the ATO cannot register tax defaults with credit rating agencies, as a bank or trade creditor might, but there are tentative signs that the ATO would like that information made public. ATO Second Commissioner Geoff Leeper said in 2014:¹³⁶

the fact ... a debt to the tax office cannot be disclosed to the markets because of the secrecy provisions [means that] there are no credit reference consequences from being in debt to the tax office. ... This is a matter for government to consider at some point. The only way around it that we can think of is to

¹²⁴ Senate Economics References Committee, n 11, recommendation 4.

¹²⁵ Senate Economics References Committee, n 11, recommendation 14.

¹²⁶ Senate Economics References Committee, n 11, recommendation 39.

¹²⁷ See <https://e-justice.europa.eu/content_insolvency_registers-110-en.do>: “Insolvency registers are a very important source of information of a legal nature for facilitating daily tasks of citizens, legal professionals, state authorities, companies and other interested parties. They facilitate access to official and trusted insolvency-related information to banks, creditors, business partners and consumers. This information enhances transparency and legal certainty in European Union markets. ... the core services provided by all registers are to register, examine and store insolvency information and to make this information available to the public.”

¹²⁸ See <<https://www.gov.uk/government/news/launch-of-the-new-companies-house-public-beta-service>>.

¹²⁹ See <<https://www.gov.uk/government/news/free-companies-house-data-to-boost-uk-economy>>.

¹³⁰ *Privacy Amendment (Enhancing Privacy Protection) Act 2012* (Cth).

¹³¹ D Francis, “Summary of the Impact of the Amendments to the Privacy Act” (2014) *Credit Management in Australia* 8, 8.

¹³² *Privacy Act 1988* (Cth) Sch 1.

¹³³ *Privacy Act 1988* (Cth) s 20L(2), Sch 1, Australian Privacy Principle 9.

¹³⁴ *Privacy Act 1988* (Cth) Pt IIIA.

¹³⁵ According to a survey of credit managers who were members of the Australian Institute of Credit Management in February 2016, 96.19 per cent of credit managers agree or strongly agree that “[h]aving the ATO list all unpaid tax by commercial entities would significantly enhance my credit approval/declining decision making.” Survey on file with author.

¹³⁶ Australian Government, House of Representatives, Official Committee Hansard, Standing Committee on Tax and Revenue, 28 February 2014, 24.

propose that the Commonwealth as an entity have the ability to advise a credit market, “Geoff owes \$41,000,” without disclosing the nature of that debt.

The significance of publicly available tax default information is that unpaid taxes are often an early sign of the precariousness of a company and its likelihood of defaulting on other debts. If credit rating agencies could include this sort of information in its advice to prospective lenders and trade creditors, one significant incentive towards phoenix activity – its invisibility – might be undermined.

PRIVATISATION OF ASIC’S REGISTRY AND TREASURY’S PROPOSAL FOR ASIC INDUSTRY FUNDING

Unfortunately, Australia appears headed for the opposite approach in terms of making ASIC registry data publicly available, both with the government’s tender to run ASIC’s registry as a private business,¹³⁷ as well as Treasury’s consultation paper on industry funding for ASIC’s operations.¹³⁸ The outcomes of these two processes are not yet known but they show a worrying tendency against free and transparent access to company information. A private registry operator, while committed by the tender terms to “open and equal access”,¹³⁹ will necessarily charge for the majority, if not all, the information it provides, as ASIC does with the majority of its information at present. It appears that the drive towards registry privatisation is based on a need to upgrade ASIC’s computing capabilities without the cost of that process being borne by the government. The Department of Finance has stated that:¹⁴⁰

The Registry’s capacity is currently significantly limited due to its existing IT solution. The current IT solution is “fit for purpose” but some systems lack the functionality to make significant or quick improvements to user experience.

The Registry’s existing technology has certain systems, some of which are over 25 years old which creates limitations on service levels. This is due to some registrations being paper based, and particular data cannot be linked across registers. Currently there is limited ability to develop value added products/services under the existing IT solution.

The Government believes that the involvement of the private sector has the capacity to unlock significant value within the Registry and deliver considerable benefits to the economy.

The ASIC industry funding consultation paper, while acknowledging ASIC’s view that “[r]egistered liquidators are gatekeepers in the financial system”,¹⁴¹ nonetheless proposed to charge liquidators approximately \$9 million in 2016–17 for being provided by ASIC with guidance and being subject to surveillance and enforcement actions.¹⁴² ASIC’s own submission to the Treasury consultation paper argued against the cost of its regulatory activities being passed on to the public as a whole via general taxation,¹⁴³ on the basis that:¹⁴⁴

only those consumers who use the products of regulated firms will share the costs of paying for ASIC’s regulatory activities. As a consequence, general taxpayers, many of whom do not use or benefit directly from some of ASIC’s regulatory activities, are not burdened with these costs.

¹³⁷ Australian Government, Department of Finance: “The Government announced in the 2014–15 Budget that it would commission a scoping study into future ownership options for the operation and ownership of the registry functions of the Australian Securities and Investments Commission (ASIC) Registry”: see <<http://www.finance.gov.au/procurement/scoping-studies/asic-faqs>>. Expressions of interest closed on 19 October 2015. Indicative bids closed on 23 February 2016.

¹³⁸ Australian Government, Treasury, *Proposed Industry Funding Model for the Australian Securities and Investments Commission*, Consultation Paper (2015). Submissions closed on 9 October 2015. See <<http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2015/Proposed-industry-funding-model-for-ASIC>>.

¹³⁹ See <<http://www.finance.gov.au/procurement/scoping-studies/asic-faqs>>.

¹⁴⁰ See <<http://www.finance.gov.au/procurement/scoping-studies/asic-faqs>>.

¹⁴¹ Australian Government, Treasury, n 138, 49.

¹⁴² Australian Government, Treasury, Attachment D.

¹⁴³ Australian Securities and Investments Commission, *Proposed Industry Funding Model for the Australian Securities and Investments Commission*, Consultation Paper (2015).

¹⁴⁴ Australian Securities and Investments Commission, n 143, [17 (a)].

While this may be true for some of ASIC's other regulatory responsibilities,¹⁴⁵ it fails to recognise that liquidators, playing a gatekeeper role for the government, are assisting ASIC with its own work as a corporate regulator and that the general public benefits from the contribution made by liquidators. Any additional impost on liquidators necessarily must be passed on to their paying clients – insolvent companies with some assets – and exacerbates the cross-subsidisation that already occurs for assetless administrations. In essence, a levy on liquidators for ASIC's services will be borne by the creditors of companies which enter liquidation with assets.

CONCLUSION

The challenge for those engaged in phoenix activity research and reform is not to throw the baby out with the bathwater. Prohibiting business rescue by former company controllers has the potential to do more harm than good, quite apart from encouraging hidden avoidance behaviour. Placing substantial hurdles in the way of all those seeking incorporation would also thwart highly desirable innovation and consequent benefits to the economy. What this article recommends is a nuanced approach involving minor additional paperwork for all prospective directors, additional reporting on the circumstances of insolvency, and greater transparency to aid self-protection and enforcement activities.

At present, phoenix activity is virtually invisible, with no regulator keeping track of whether the controllers of a failed company start one or more further companies. More detailed data gathering at the time of incorporation, together with proof of identity, would simplify ASIC's task in monitoring directors who might warrant disqualification. Fuller disclosures by external administrators and more thorough RATA reporting would also arm both ASIC and liquidators with the information they need to bring enforcement action. Providing free information to liquidators would allow them to support ASIC's own efforts more than they are currently able to do. Given the limited resources available to both ASIC and liquidators, it is vital that their tasks are made as straightforward as possible. Affording prospective creditors the means to protect themselves against phoenix operators lessens the burden on gatekeepers and has the potential to reduce the financial impact of phoenix activity on the economy.

Allowing ASIC to differentiate incorporations based on improved information opens the way to measures that reduce the ease and profitability of multiple phoenix activity, whether involving illegality or an inept serial entrepreneur. For example, the government could legislate to require the prospective director of a fifth company to undertake compulsory education or quarterly financial reporting. A higher cost of incorporation could be charged for a 10th company. The ATO could be alerted to seek a security bond where there were three previous failures associated with a person. The FWO could add the new company's name to a list of employers to watch.

As an aside, there has been much discussion in recent years about the possibility of allowing pre-packaged administrations (pre-packs) in Australia,¹⁴⁶ with fears being raised that they might shield illegal phoenix activity where the pre-arranged sale is to a related party.¹⁴⁷ Greater information about directors and their previous dealings could alleviate these fears by helping to establish which pre-packs are genuinely arm's length and which require closer scrutiny. The present general lack of knowledge about a director's identity and prior corporate history casts a shadow over all potential pre-packs.

Greater transparency is not the sole answer to a problem as complex as phoenix activity. However, as a relatively low cost measure, it has the capacity to significantly improve deterrence and enforcement in an environment that has struggled for two decades with an effective strategy to overcome this costly behaviour.

¹⁴⁵ Australian Securities and Investments Commission, n 143, [2].

¹⁴⁶ See, eg, Productivity Commission, n 39, recommendation 14.3.

¹⁴⁷ See, eg, the extensive discussion of sales to connected parties discussed by P Walton and C Umfreville, *Pre-Pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration: Final Report to the Graham Review* (University of Wolverhampton, 2014).