# THE INSOLVENCY REVIEW

ISSUE 02 - MAY 2021

In Focus:
**New Insolvency Processes**

Personal Insolvency:
**Key Trends March Qtr 2021**

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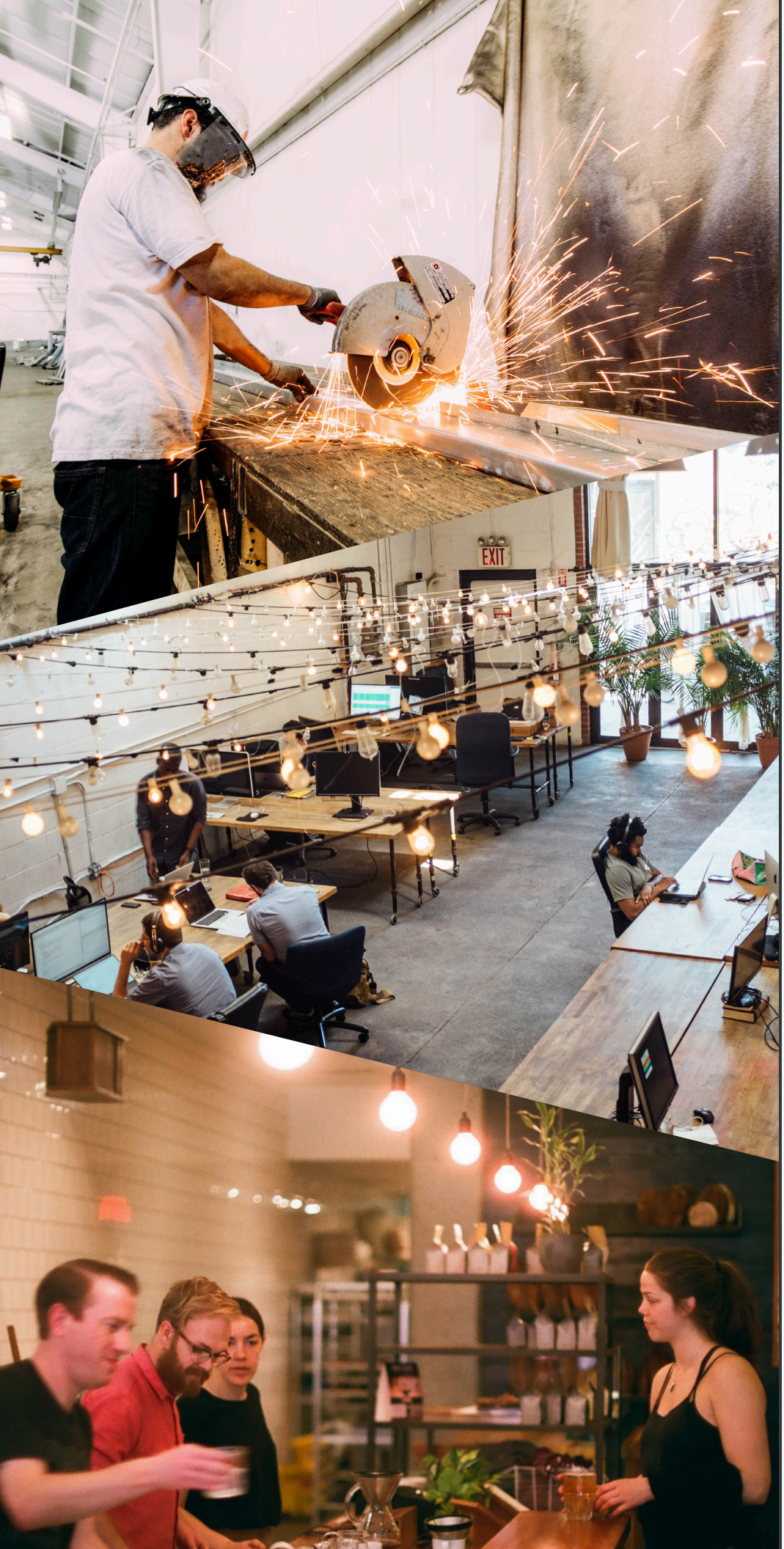


# WELCOME

Welcome to the second issue of The Insolvency Review.

2021 is well and truly underway and it's a brave new world. Snap lockdowns and social distancing are here to stay for the foreseeable future and, with many Government support measures coming to an end, businesses will be gaining a clearer understanding of their true position.

In this issue, we take a closer look at the new insolvency processes introduced, with more cost effective solutions providing better opportunities for businesses to recover and get back on track.

Our overview of the personal insolvency landscape provides a snapshot of key trends nationally and on a per state basis and predictions as we move into the new financial year.

As always, we encourage feedback and commentary so please get in touch.

Enjoy this issue.

Terry van der Velde
Managing Director
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# "Time is of the essence. Seeking advice early can be instrumental in securing a superior outcome."

Without a doubt, the last 12 months has served up more challenges than most businesses can handle. Comparatively, Australia has handled the pandemic and economic fallout better than most countries, however, the long term effects are still unknown.

With many stimulus and protection measures introduced by the Federal Government having now come to an end, companies will again start to feel the pressure from creditors, with many only now getting a clear understanding of their position.

It's been no secret that, given the measures introduced at the height of the pandemic, the number of insolvencies have decreased substantially. ASIC statistics show that the number of insolvencies YoY from 2019 to 2020 saw a reduction of 40.6% with 3381 fewer companies entering external administration in 2020 than in the previous year.[1]

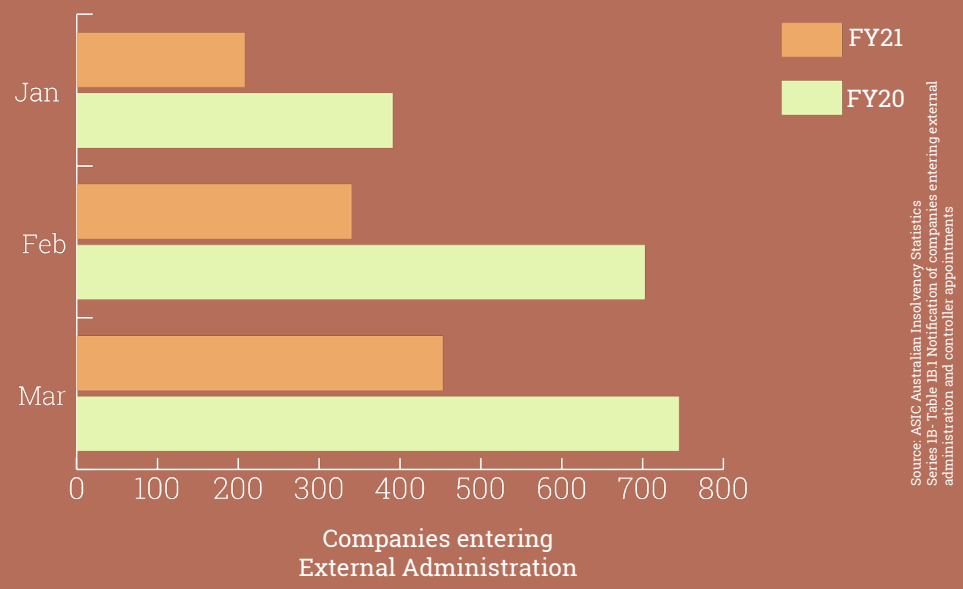
Initial figures reported for the first quarter of 2021 show that the downward trend has continued into the new year (see Fig. 1). There has however been an increase in the percentage of businesses utilising the Voluntary Administration process. Statistics show that:

- 19.6% of external administrations for the first quarter of 2021 were Voluntary Administrations
- 2020 figures show only 15.8% of all external administrations in the first quarter were Voluntary Administrations [2]

Given the introduction of two new insolvency processes to support businesses in the Simplified Liquidation and Small Business Restructuring Process, figures suggest that early adoption rates are lower than expected, with businesses instead choosing to go down a more traditional administration pathway to assist with recovery.

From an industry perspectve, research from the University of Melbourne in May 2020 reported that 28% of the Australian workforce were employed in the worst affected industries in the pandemic.[3] Those industries which were directly adversely affected include Food and Beverage services, Air and Space Transport, Heritage Activities, Creative and Performing Arts and Sports and Recreation Activities. Reports from the Australian Bureau of Statistics however show that by January 2021, employment levels had almost completely recovered with 93% of jobs lost recovered compared to pre-covid levels.[4] There has also been an increase in business confidence as a whole with 46% of businesses expecting to meet their financial comitments easily over the next three months compared to only 23% in August 2020.

**Fig. 1**




In reality, the next six to twelve months will be crucial, with the expected backlog of regular run-rate insolvencies returning as relatively normal business activities resume across industries. The overall sentiment is that many businesses which were only barely clinging to life prior to the pandemic will now unfortunately meet their fate, resulting in a surge of insolvencies nationally.

**"With the stimulus and protection measures introduced by the Federal Government coming to an end, companies may face pressure from creditors once again."**

**Travis Olsen**
Associate Director

1 ASIC Australian Insolvency Statistics Series 1A April 2021
2 ASIC Australian Insolvency Statistics Series 1B April 2021
3 The Melbourne Institute (2020, May). *Who's hit hardest by the economic effects of COVID-19? ISSN 2653-004X*
4 ABS - One year of COVID-19: Aussie jobs, business and the economy March 2021

# New Insolvency Processes: Simplified Liquidation & Small Business Restructuring Process

In the wake of the COVID-19 pandemic and in an effort to further assist businesses, the Federal Government introduced two new formal insolvency processes, the Simplified Liquidation and Small Business Restructuring Process.

The Simplified Liquidation (**SL**) process was designed to reduce the cost and time involved in completing the liquidation process and is essentially, a streamlined version of a Creditors' Voluntary Liquidation (**CVL**).

The SL process can be adopted after a company has been placed into a CVL where the company meets certain prescribed eligibility criteria.

In order for a company to be eligible, the company must:

- be unable to pay its debts within 12 months after the liquidation commences;
- have total liabilities of less than $1 million (not including contingent liabilities);
- ensure all its tax lodgements are up to date and
- have not used the simplified liquidation process or been under restructuring in the last 7 years

In addition, the directors of a company must provide a declaration, within 5 business days after the liquidation commences, that they believe the eligibility criteria for the simplified liquidation process are met.

The streamlined nature of the SL process offers some benefits over the CVL process including:

- No creditor meetings;
- Reduced reporting requirements;
- Cheaper and more convenient communication;
- Fewer circumstances in which liquidators can clawback monies and
- A faster and more cost effective process with potential for expedited wind-up and deregistration of the company

The Small Business Restructuring Process (**SBRP**) is the second formal insolvency process introduced in 2021. The SBRP allows directors and management to remain in control of the company (under the supervision of a restructuring practitioner).

The purpose of the SBRP is to provide directors and the company time to put forward a plan to creditors to pay off their liabilities, in full or in part, within a period not exceeding 3 years.

For a company to be eligible for the SBRP, the following criteria must be met:

- the company must be insolvent or likely to become insolvent;
- the company must have liabilities less than $1 million;
- the company, or a director of the company, must not have previously used either the SBRP or simplified liquidation process in the last 7 years and
- tax lodgements and employee entitlements must be up to date

Only directors of the company can propose a SBRP and must choose a restructuring practitioner (who must also be a Registered Liquidator).

The Restructuring Practitioner determines if the company is eligible and will assist to develop the plan. They will also develop the remuneration proposal, which is set at a fixed amount for the proposal period.

The company has 20 business days to develop and propose the plan to creditors, during which time the company has the benefit of a moratorium on most types of security enforcement.

Creditors will then have 15 business days to vote on the plan, which requires support from more than 50% in value of unrelated creditors in order to be approved.

Once the plan is approved, the company can continue to trade in the ordinary course of business while the plan is administered by the Restructuring Practitioner. The plan must operate for no more than three years.

Whilst these new insolvency processes go a long way to provide support for businessess, they are not a silver bullet and existing insolvency processes may be more suitable depending on the cirumstances.

It's important to understand that eligibility is a strict test and is criticial to evaluate prior to commencing any new process.

Given the unique nature of each company's financial situation and the complexities of the legislation, seeking advice at the earliest opportunity can provide the best outcome by way of providing multiple options that may exist should they eventually be required.

**"There is no free ride in business. Business owners should expect to repay fixed overheads incurred whilst their business is not operating at capacity or in hibernation and should consider the impact this will have on future cash flow."**

**David Stimpson**
Executive Director

# PERSONAL INSOLVENCY

The temporary changes to bankruptcy law in March 2020 were introduced as part of the Federal Government's wider economic response to the COVID-19 pandemic. The outcome was as expected, providing relief for many individuals in a very challenging time and subsequently leading to a decrease in personal insolvencies nationally.

The downward trend continued into 2021 with a 52.9% decrease YoY for the March quarter, down to 2545 personal insolvencies. (see Fig. 2). Figures were also down in all states and territories with the most significant decrease shown in Victoria, with a decrease of 59.9%.

2021 Key Stats (see Fig. 3) :

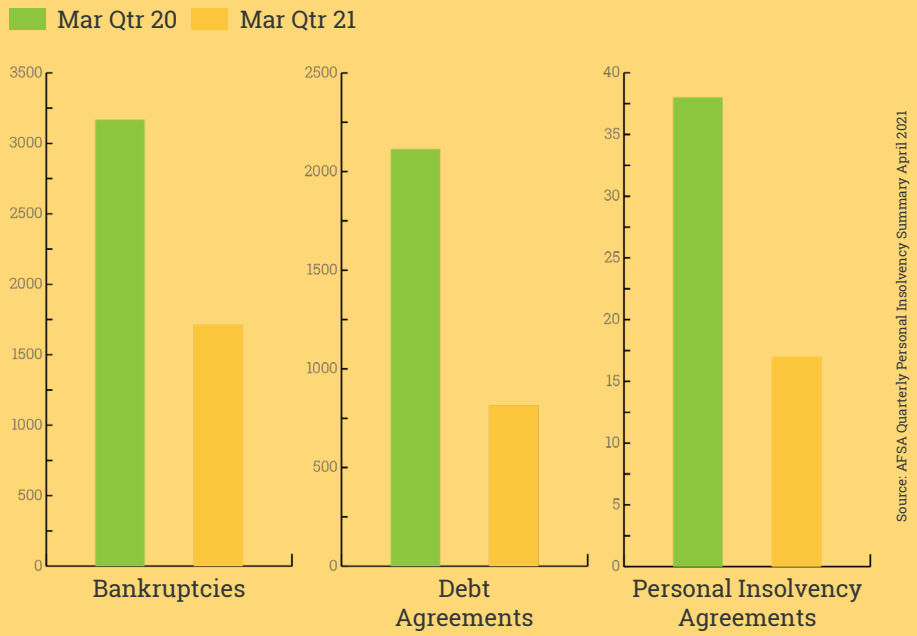
- Bankruptcies (Part IV & XI) - 1,712 down from 3,168 in March 2020
- Debt Agreements (Part IX) - 816 down from 2,113 in March 2020
- Personal Insolvency Agreements (Part X) - 17 down from 38 in March 2020[1]

There has been a slight uptick in the number of personal insolvencies over the quarter with a rise of 5.8% compared the December quarter 2020.[2]

Of the 1,712 bankruptcies reported for the March quarter this year, 30.8% were business related, falling from 37.3% in the March quarter of 2020.

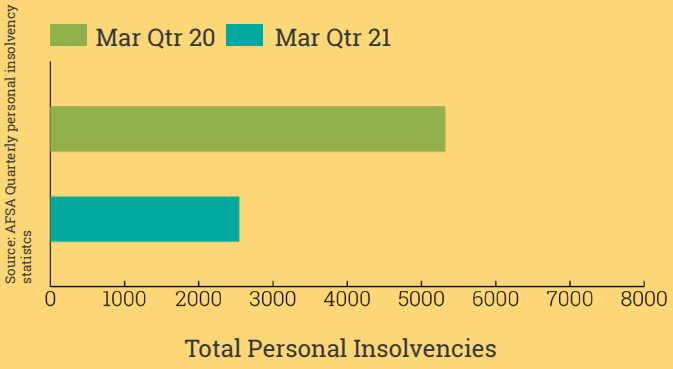
Conclusion of the Federal Government's JobKeeper program at the end of March along with the ATO officially recommencing recovery processes for tax debt, will see many individuals likely facing further financial pressure.

**Fig. 3**




> "As creditors are the ones who ultimately decide the fate of the debtor, it is wise for the debtor to put themselves in creditor's shoes."

**Fig. 2**




## What are the different types of Personal Insolvency?

**The most common types of personal insolvency are known as bankruptcy, personal insolvency agreements (PIA) and debt agreements. SV Partners also provides statutory trustee and administration of deceased estates services.**

1 AFSA Quarterly Personal Insolvency Summary April 2021
2 AFSA Media Release - Statistics, 20 April, 2021

# 2545

2545 new personal insolvencies in Australia in March Qtr 2021 **with a total decrease of 52.9% YoY**

Personal insolvencies YoY for the March quarter on a per state basis have followed the downward trend of national figures.

The total number of business related personal insolvencies decreased by more than half YoY for the March quarter, with a total of 592 down from 1,350 in March 2020.

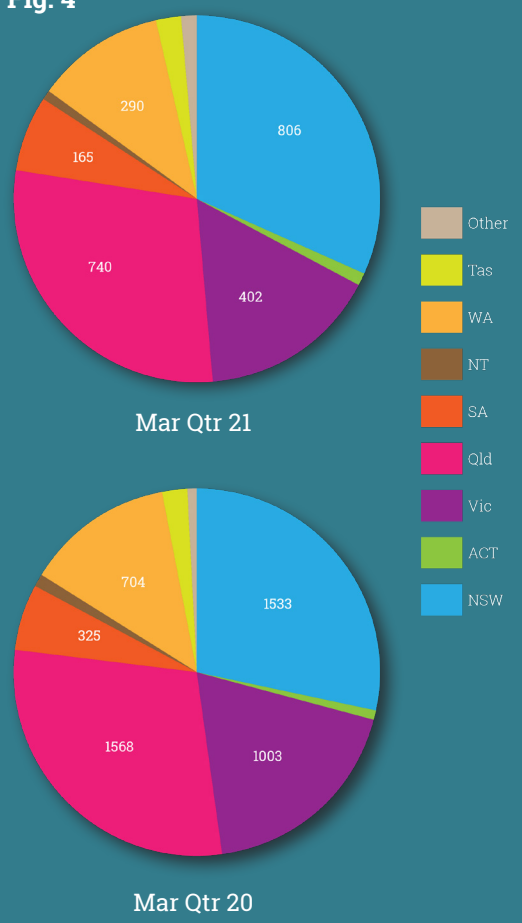
Similarly for non-business related personal insolvencies, there were a total of 1,953 compared to 4,054 in the March quarter of 2020.

Key stats (see Fig. 4):

- 806 people entering personal insolvency in New South Wales down from 1,533 in March 2020
- 740 entering personal insolvency in Queensland down from 1,568 in March 2020
- Victoria reported 402 people entering personal insolvency down from 1,003 in March 2020 [1]

With the conclusion of many Government support measures, the increase in numbers over the March quarter will likely continue into June and for the foreseeable future, as many individuals take stock of their true financial position.

**Fig. 4**




Source: AFSA Quarterly personal insolvency statistcs

1 AFSA Quarterly Personal Insolvency Statistics Time Series - April 2021

# The Outlook
# WHAT'S NEXT?

2020 was a year unlike any other in recent memory. The speed with which the pandemic took hold and subsequent economic impact was truly a once in a generation global event. As we continue to try and control the spread of the virus, limit further economic impacts and adjust to the new normal, many are wondering what's next?

The International Labour Organization estimates that the number of working hours lost in 2020 due to the economic impacts of COVID-19 was the equivalent of 255 million full time jobs.[1] In response to the pandemic, the Australian Government implemented the most comprehensive economic support measures in our nation's history with overall support totalling $507 billion, inclusive of the JobMaker Plan.[2] Further, the ATO has made every indication that it is to resume recovery efforts for unpaid debts with a reported debt book of $53 billion.

The transition out of the JobKeeper program will be a difficult but necessary one and will provide clarity on the true financial position of many businesses, some of whom were in financial distress prior to COVID-19. The long term implications of such a significant national debt are sure to be worrying to many and it is likely that everyday Australians will have to carry the burden, in one form or another, of repaying the money used to keep the economy alive during the pandemic.

The introduction of new insolvency processes to support business and improve the chance of recovery are welcome however, businesses need to act early when seeking to address financial difficulties. Being honest and upfront with creditors as to the reasons for difficulties can increase the likelihood of a successful outcome and the long term viability of a company.

1 ILO Monitor: COVID-19 and the world of work. Seventh edition
2 Budget 2020-21 Fact sheet: The Economic Recovery Plan for Australia

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