

## Article Information

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## New COVID-19 Treasury Amendments: Insolvency and Financial Hardship

**As the COVID-19 pandemic escalates and the Australian Government implements measures to address the ongoing health crisis, the toll on the Australian economy will increase.**

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In recognition of the financial hardships faced by Australians and Australian businesses over the next few months, the Australian Government has passed the *Coronavirus Economic Response Package Omnibus Bill 2020* which makes temporary amendments to the *Corporations Act 2001* (Cth) (**Corporations Act**) and *Bankruptcy Act 1966* (Cth) to lessen the financial impact of the pandemic on individuals and businesses.

### Key Amendments

The *Coronavirus Economic Response Package Omnibus Act 2020* contains the following amendments, which came into effect on 25 March 2020:

#### Minimum debt threshold - statutory demands and bankruptcy notices

The minimum debt threshold for issuing statutory demands and bankruptcy notices has been increased to \$20,000 (up from \$2,000 for statutory demands, and \$5,000 for bankruptcy notices). This temporary amendment will apply for a period of 6 months.

#### Debtor response period - statutory demands and bankruptcy notices

The period for debtors to respond to statutory demands and bankruptcy notices has been increased to 6 months (up from 21 days for both statutory demands and bankruptcy notices). There is a presumption of insolvency (for a debtor company) or an act of bankruptcy is committed (for a debtor individual) if the debtor fails to respond to the statutory demand or bankruptcy notice within the required time. The 6 month response period will apply for 6 months, commencing on 25 March 2020.

In essence, these measures will freeze the ability to commence proceedings to wind up a company or put an individual into bankruptcy for a period of 6 months, by which time, presumably the worst of the pandemic will have passed, the government-imposed restrictions on daily life and business will be loosened, and business and individuals will be better capable of dealing with such issues.

#### What effect will these amendments have on ipso facto provisions?

Contracts often contain provisions (also known as 'ipso facto' provisions) entitling a party to terminate the contract where the other party experiences an insolvency event. Generally, an 'insolvency event' is defined to include circumstances where a party is unable to pay its debts when they fall due or where a party is deemed unable to pay its debts under any applicable legislation.

The temporary amendments proposed in response to the COVID-19 pandemic will only affect the operation of ipso facto provisions to the extent that such provisions expressly include a reference to the presumption of insolvency where a debtor fails to respond to a statutory demand within the response period. In those circumstances, even where the right to terminate exists, it will still be necessary to wait for the new response period (6 months) to expire prior to exercising rights

under an ipso facto provision. As statutory demands are not a matter of public record, it is usually impossible to know if a debtor has failed to comply with a statutory demand issued by another creditor and whether ipso facto rights arise as a result.

However, it is important to note that, as a result of the amendments to the Corporations Act which came into effect in 2018, subject to certain exceptions, a party is unable to rely on a contractual right to terminate solely due to the appointment of a voluntary administrator or receiver to the counterparty, or its entry into a scheme of arrangement, for a set period of time (dependent on the nature of the contract and the insolvency event). As a result, we do not contemplate that the temporary amendments to the Corporations Act themselves will have a significant effect on a party's ability to rely on ipso facto provisions, except to the extent that any of the exceptions to the moratorium on the enforcement of ipso facto provisions apply.

### **Temporary safe harbour provision**

Directors of companies will be afforded temporary relief for a period of 6 months from personal liability for insolvent trading where the company incurs debts in the ordinary course of the company's business. This relief will only apply to debts incurred during the 6 month period starting on the commencement of this amendment, and therefore will not provide relief where a company was insolvent prior to the commencement of the provision.

The Explanatory Memorandum to the Bill states that a director will be taken to incur debts in the ordinary course of business where it is "necessary" to facilitate the continuation of the business. The requirement for the debt to be "necessary" would seemingly apply a high threshold for directors to satisfy in order to rely on this temporary safe harbour provision.

The new safe harbour provisions also note that they will not apply to companies and debts incurred in certain circumstances prescribed by the regulations, however the relevant regulations have not yet been published.

In these extraordinary and unexpected times, it is vital that the Federal and State Governments implement measures to promote effective business management with the aim of keeping businesses afloat. These temporary amendments will assist directors in managing their business through the pandemic, and provide individuals and businesses with breathing room before having to deal with statutory demands and bankruptcy notices.

Where a business is in a particularly vulnerable financial state, it should devise a plan immediately for the turnaround of the business and have this approved by an independent insolvency professional.

### **Key Takeaways**

The Australian Government has implemented temporary amendments to the *Corporations Act 2001* (Cth) and *Bankruptcy Act 1966* (Cth) to lessen the impact of the current economic situation as a result of the COVID-19 pandemic. These amendments include:

1. Increasing the minimum debt threshold for statutory demands and bankruptcy notices to \$20,000;
2. Increasing the period for debtors to respond to statutory demands and bankruptcy notices to 6 months;
3. Temporary relief from director liability for insolvent trading.

These amendments commenced on 25 March 2020.

*Piper Alderman is assisting clients on the spectrum of legal issues arising from the pandemic. Please view our [COVID-19 Resource Hub](#) for more information on areas including **employment, industrial relations, construction law, insolvency and property**.*