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Australian Government
Australian Financial Security Authority
PERSONAL INSOLVENCY REGULATOR

In this issue

Did you see?

Our recent AFSA news article 'Getting tough on

Objection to discharge practice direction now published

The June 2018 PIR newsletter included an article giving guidance to trustees and their staff on use of the objection to discharge regime.

We've now published an Inspector-General Practice Direction (IGPD7) on our website to give guidance on objections to discharge from bankruptcy and the Inspector-General's expectations of trustees with respect to the regime.

Varying and terminating debt agreements—debtor rights and RDAA responsibilities

The Inspector-General in Bankruptcy (IG) has recently received feedback from debtors via our Debt Agreement team (DAt) and complaints via regulation, about registered debt agreement administrators (RDAAs) refusing their requests to process variation and termination proposals.

It would appear that certain RDAAs wrongly believe they have discretion to assess variation or termination requests by debtors, including deciding whether creditors are likely to accept or reject such proposals.

Anecdotal information suggests that such actions by RDAAs are motivated by concerns that the proposed variation or termination will adversely affect fee recovery under the debt agreement.

The IG takes this issue seriously, and takes this opportunity to clarify the following rights of debtors and duties of RDAA under the *Bankruptcy Act 1966* (the Act).

Debtor rights

The right of debtors to propose a variation or termination of their debt agreement is outlined in Official Receiver Practice Statement (ORPS) 11—Debt agreements (paragraphs 11.2 and 11.16 respectively) published on AFSA's website.

untrustworthy advisors'

11. Variation and termination

Proposal to vary a debt agreement

11.1. A proposal to vary a debt agreement generally arises from a change in the debtor's circumstances, for example:

- *a change in income resulting in a reduction or increase in the amount they can afford*
- *an increase in the number of dependants, such as an additional child*
- *the loss of a partner's income*
- *an increase in household expenses*
- *a loss on repossession of secured property during the debt agreement, resulting in an increased value of provable debts*
- *an increase in income from a new job, resulting in an ability to increase payments*
- *support from a third party to assist with payments*
- *the ability of the debtor to offer up a lump sum to complete the agreement.*

11.2. Only the debtor or, in limited circumstances, an affected creditor, may lodge a proposal to vary a debt agreement. An administrator may only lodge a proposal to vary if they are also an affected creditor.

Proposal to terminate a debt agreement

11.15. A debtor or creditor may propose termination of a debt agreement. The following are examples of the types of situations that may prompt a proposal to terminate:

- *the failure of the debtor to start or maintain payments with little likelihood of completing the debt agreement*
- *a change to the debtor's circumstances where he or she can no longer afford payments and a variation to reduce payments is not feasible*
- *material non-disclosure of employment or income that would have affected the creditors' original decision to support a debt agreement*
- *a material reduction in the estimated dividend to creditors because of significant undisclosed debt*
- *a material omission of divisible property that would have affected the creditors' original decision to accept the debt agreement.*

11.16. Only a debtor or creditor who is a party to the debt agreement may lodge a proposal to terminate a debt agreement. An administrator my lodge a proposal to terminate when they are an affected creditor.

The above extracts from ORPS 11 explain that only a debtor or an affected creditor—in limited circumstances—may lodge a debt agreement variation or termination proposal.

RDAA duties

The duties of a RDAA are to administer the debt agreement under the Act. In this capacity, they act on behalf of, and owe fiduciary obligations to, the debtor, which include a duty to use care and skill and to be trustworthy.

This is specifically recognised in the respective Codes of Professional Practice for members of the:

- Personal Insolvency Professionals Association Ltd (PIPA) (clauses 2.1–2.2)
- Australian Restructuring Insolvency & Turnaround Association (ARITA) (clauses 2.2, 2.7).

Regardless of whether a RDAA is a member of PIPA or ARITA, the principles expressed in the respective codes of these professional bodies is consistent with the general law and the IG's expectations.

In practice, the fiduciary obligations require a RDAA not to place their interests ahead of the debtor's when a variation or termination request is received.

For instance, it would be improper for a RDAA to refuse to submit a debtor's variation or termination proposal request to the DAt, because it would be likely to reduce the expected fees payable to the RDAA under a debt agreement.

Similarly, it would be improper for a RDAA to refuse to submit a debtor's variation or termination proposal to the DAt because the RDAA believes that it would not be accepted by creditors.

While a RDAA has an important role in administering the debt agreement and providing information to debtors that is objective, responsive and professional—including on their rights to request a variation or termination—the decision to do so ultimately rests with the debtor and/or creditors.

Although currently, there is no positive duty imposed on a RDAA to prepare a variation or termination proposal for the debtor, the IG expects that most will do so to assist their clients when their circumstances change for one or more reasons outlined in ORPS 11 (paragraph 11.1).

Further, where a RDAA is unable or unwilling to perform this function for a debtor, then the IG expects that this be disclosed to the client before they agree to nominate the RDAA to ensure that they are fully informed and can decide whether another administrator may better suit their needs.

This is consistent not only with IGPD 22—Effective practitioner communication, but also ensures that RDAAs uphold high profession standards and stakeholders maintain integrity in the personal insolvency system.

A RDAA who deliberately or persistently refuses to submit a debtor's variation or termination proposal to the DAt, will be investigated by AFSA Regulation and may be subject to disciplinary action by the IG if found to have breached their duties.

Paul Eric
Assistant Director — Regulation

New Australian Financial Complaints Authority launched

On 1 November 2018, a new external dispute resolution (EDR) scheme called the Australian Financial Complaints Authority (AFCA) was launched to deal with complaints from consumers in the financial system.

AFCA replaces three existing financial services EDR schemes:

- the Financial Ombudsman Service
- the Credit and Investments Ombudsman
- Superannuation Complaints Tribunal.

Now consumers and small businesses with less than 100 employees will be able to make complaints to AFCA regarding matters of up to a $1 million value (other than superannuation complaints or complaints arising from a credit facility provided to a small business, for which there is no limit), and order compensation of up to $500,000.

Some of the types of complaints that AFCA will hear include:

- complaints about inappropriate or incorrect advice from a financial advisor
- complaints about an insurer's decision to reject a claim
- complaints about the amount deemed to be payable under a superannuation death benefit.

Implications for personal insolvency practitioners

All financial services providers are required to be AFCA members, including financial services licensees, credit licensees and regulated superannuation funds.

This means that personal insolvency practitioners (such as registered debt agreement administrators) who are also a credit or financial services licensee, must be an AFCA member, and are subject to its EDR scheme.

Implications for debtors and bankrupts

Debtors or bankrupts may request AFCA to intervene and investigate in an effort to resolve disputes between parties, if they have a complaint about:

- credit, finance and loans
- insurance

- banking deposits and payments
- investments and financial advice
- superannuation.

If a complaint does not resolve between the parties, AFCA will decide an appropriate outcome.

Decisions made by AFCA can be binding on the financial firm involved and may include awarding compensation for losses suffered because of a financial firm's error or inappropriate conduct.

AFCA has a factsheet available on its website for insolvent consumers. The factsheet explains that AFCA can only consider a bankrupt's complaint with the consent of their bankruptcy trustee (except where the complaint relates to non-vesting superannuation interests).

It is important to note that the trustee is not obliged to (and may refuse to) provide consent to a bankrupt seeking to lodge a complaint with AFCA. An example of where a trustee refused to give consent for a bankrupt to lodge a complaint was considered in *Mann v Condon* [2013] FCCA 780.

Further details about AFCA is available on their website.

Paul Eric
Assistant Director — Regulation

The usefulness of service documents

AFSA Enforcement is committed to working with trustees to achieve quality outcomes and to foster confidence in the personal insolvency system. We recognise that this includes working with trustees, wherever possible, to try achieve quality outcomes both inside and outside the courtroom.

However, as is the case with any regulatory agency, AFSA Enforcement can only investigate matters where there is adequate evidence of the suspicion of the committing of an offence—section 12(1)(bc) of the *Bankruptcy Act 1966* (Bankruptcy Act).

This involves an assessment of the witness accounts and physical evidence that arise during the course of a trustee's investigation. Anecdotally, a common sticking point between AFSA Enforcement and trustees is an assessment about the 'good service of documents'.

Key points

- In civil litigation, the service of documents is primarily about establishing that the giver of notice has abided by the rules set out, that would form the basis of good notification.
- For the purpose of a subsequent criminal prosecution, the service of notice is about having good available physical evidence, which would prove the knowledge or intention of the receiver of notice.
- If an allegation involves a person not complying with an obligation, request or direction, AFSA Enforcement must prove 'beyond a reasonable doubt' that the person was aware of the obligation or request.
- Examples of service include personal service, delivery of notice or documents with a follow-up phone call, and registered post.

Bankruptcy trustees are generally familiar with the nature of litigation, which permits them to appreciate service of notice obligations in the course of civil recovery action. However, the purpose and use of service of documents in the course of administering a bankrupt estate varies between civil and criminal litigation. This article seeks to explore the question of service, the usefulness of service, and the difference in service between civil and criminal proceedings.

Civil proceedings

The Civil Procedure Rules applicable to each Court set out the rules for service and the conditions under which substituted service can be used. The broad purpose of these rules is to ensure that the respondent understands that there is an action against them, and to allow an opportunity to prepare a defence.

Good service as it is able to be demonstrated in civil Courts can vary subject to specific Commonwealth legislation. Two examples that insolvency accountants may be familiar with are the following:

1. s 109X of the *Corporations Act 2001* (Corporations Act), requiring the service of documents on the registered office of a corporation
2. regulation 16.01 of the Bankruptcy Regulations 1996, which prescribed the way service of notices or documents can occur.

In civil disputes, these provisions act to support the civil procedure rules applicable in each Court. For example, a civil dispute arising out of the service of notice to a banking institution by a trustee for the purpose of s 125 of the Bankruptcy Act, or the delivery of property or records in respect a request under s 129 of the Bankruptcy Act, would rely upon perhaps both these Corporations Act and Bankruptcy Regulation provisions to establish service, and from which, liability of the party subject to any subsequent civil claim might result.

Criminal proceedings

A criminal offence requires proof 'beyond reasonable doubt' of specified physical conduct (physical element), and the state of mind of the offender (fault element).

These two key components must exist in the manner prescribed by an offence provision and by reference to the Criminal Code. The degrees of intentionality vary based on the construction of the specific offence provision. The relative test for intentionality is known as the fault element. Two common examples of fault elements are 'intention', which requires evidence of the state of mind of the alleged offender at the time of the conduct, and the lesser standard 'recklessness'. The difference between these two elements is equivalent to the difference between an active understanding of what was required (I know I need to do A, but I'm going to do B), and that the person ought to have understood what was required but was reckless (I was given a document that set out that I should do A, but I didn't read it, and I did B).

The mere act of sending a letter to a last known address, which would constitute good service for the purposes of a civil action, does little to prove the 'intention' or 'recklessness' fault element requirements. The physical conduct may exist, however, (in the absence of an admission) to prove the degree of intent there needs to be evidence about what the alleged offender was thinking. Primarily, this is achieved by of two broad forms of evidence prior to or at the time of the offending:

1. non-hearsay witness testimonies of what one person knows of the other person's intent because of what they were told or
2. physical documents and other evidence that, when put together, prove that intent.

The application of 'intention' or 'recklessness' is relative to an offence provision itself.

As an example, one of the many elements to be proven in relation to offending under s 266(3) of the Bankruptcy Act (disposal of property within 12 months prior to bankruptcy with intent to defeat creditors) would require proof that a defendant became bankrupt within twelve months after the disposal of property that is subject to the offending. Proving this element would require physical evidence that the person became bankrupt, but the need to prove that they intended to become bankrupt is absent. Proving the occurrence of the bankruptcy requires a fault element of 'recklessness' because there is no need to prove that a bankrupt intends to go bankrupt at the time they dispose of the property. It is only a requirement to prove that they ultimately became bankrupt, either voluntarily by way of debtor's petition, or involuntarily by way of creditor's petition. In essence, the bankrupt was reckless in that they did not avoid bankruptcy.

Conversely, s 267B of the Bankruptcy Act (failure of person to provide information) would require proof that a person refused or failed to comply with a notice, being a notice pursuant to subsection 6A(3), 77C(1) or sections 77CA or 139V of the Bankruptcy Act. It is logical that the notion of refusing or failing to comply, would be predicated on actual knowledge of a requirement to comply with the notice. Consequently, the higher fault element standard of 'intention' would apply here. The mere sending of a notice to a recipient would provide insufficient evidence to prove beyond reasonable doubt that the notice was received, read and understood by the recipient, such that the resulting conduct was a refusal to comply with the requirement to respond. Clearly, more substantial documentary evidence would be required to prove the knowledge of awareness of the obligation and the active decision not to comply. In the absence of this element, a prosecution will fail.

Consequently, service requirements for the purposes of making out criminal conduct in respect to particular offences under the Bankruptcy Act, are not about service at all, but rather about measuring the intent of the recipient. Frequently, mere evidence of receipt of the notice will fail to satisfy the requirement to prove intentional contravention of the law.

Practitioner guidance for service for subsequent prosecution action

There are varieties of service options for the purposes of determining intent in the event of criminal procedures. The following is a listing of evidence for the six most frequent methods we see at AFSA Enforcement, ranked from strongest to weakest:

1. **Personal service by a trustee/staff at a meeting or interview.**
   Handing a notice or obligations package direct to a person, and explaining and confirming the understanding of the requirements of the notices/obligations is the high water mark of service. This gives the opportunity for the recipients to ask questions and get clarity. Unfortunately, this option is not always convenient or cost effective. However, if the opportunity arises in the course of an administration, such that a potential recipient will attend a meeting personally, this will enable the corroboration and documentation of the recipient's knowledge and intent.
2. **Delivery of notice or documents with a subsequent telephone, email or in person acknowledgement, prior to a deadline set out in a notice.**
   Automatic email read-receipts will not satisfy an element of acknowledgement of receipt of a document, from an evidentiary point of view, as emails are often produced because of a computer program suggesting delivery has been made. It lacks evidentiary qualities of proving knowledge of the notice or its content by the recipient. A composed email reply from the recipient acknowledging receipt may be sufficient for the fault element of 'recklessness' but may not be for the fault element of 'intention', subject to who has access to the email account (a secretary may have access to an email account for a partner at a law firm, for example).
   A date for production of records commencing from a date of receipt of the notice is also always preferable to a specific date set as the deadline. If a notice sets a deadline to produce of 1 July, and the acknowledgement

of receipt is 30 June, a single day to reply and/or produce records in response to a notice will not satisfy the intention default element, particularly for the production of records. Requesting record be delivered within a certain period of receipt of the notice will ensure that an unreasonable period for production will never be a valid defence to a recipient, unless the records, by their nature, would require a substantial period to produce due to age or volume of the records requested.

3. **Service on registerd post address of a company, addressed to the proper officer.**
   Because a company is only a legal person, and the Corporations Act prescribes how notice should be received, the notice requirements for a company differ from those of a natural person for the purposes of proving fault elements.
4. **Process server for service of notice on an individual.**
   Subject to the requirements of the notice being served and whether active acknowledgement is required, a process server and affidavit of service can be an effective option.
5. **Australia Post registered post receipt.**
   A signature is good, however, being able to prove beyond reasonable doubt it is the signature of the intended recipient is difficult. In civil proceedings where the standard of proof is 'on the balance of probabilities', a Court might be satisfied by the comparison of two signatures that it is more probable than not that a person signed two documents. In criminal matters, with proof 'beyond reasonable doubt' handwriting experts sometimes might require multiple examples of a proven original signature to be able to give evidence of the matching of signatures, given that they would not be a witness themselves to the execution of a document/item in question by a defendant. In preference a signed registered post card, followed by a telephone or email confirmation would eliminate any doubt.
6. **Partial compliance by the recipient in reply to a normal postal letter.**
   If a notice requires the recipient to take several actions, and they acknowledge or provide a response to any one of them and ignore the others, this would infer receipt and acknowledgement of the letter on the conduct of the recipient.

Ultimately, a trustee may decide to mix and match these different methods of service based upon the importance of the information (and whether there are alternative sources), the available funds in an estate and the importance of the extent of prosecution for failure to comply.

If trustees have a matter that requires special consideration of issues such as these, we would be happy to discuss the evidentiary requirements of specific offence provisions of the Bankruptcy Act with trustees and their staff.

Brett Warren
Compliance Team Leader — Enforcement

Decision case notes

Read the recent decision case notes for:

- *Nugawela v Deputy Commissioner of Taxation* [2018] FCA 1457
- *Mallett v Inspector-General in Bankruptcy* [2018] AATA 3739

Nugawela v Deputy Commissioner of Taxation [2018] FCA 1457

Background

On 21 February 2017, sequestration orders—brought by the Deputy Commissioner of Taxation (DCT)—were made

against Dr Nugawela. In March 2017, Dr Nugawela commenced proceedings against the DCT, challenging:

i. the issuing of the sequestration orders
ii. the tax assessments

In May 2017, the sequestration orders were stayed. The stay ended on 19 June 2017 and so Dr Nugawela became bankrupt and a registered trustee was appointed.

On 30 June 2017, the DCT wrote to the trustee, providing notice of the March 2017 proceedings s 60(3) of the *Bankruptcy Act 1966*. The trustee was given an 'extension of time' by the DCT (essentially withdrawing the original notice) and gave a fresh one on 21 July 2017. On 29 August 2017, the trustee wrote to the DCT stating he had elected not to continue the proceedings. On 18 October 2017, the DCT and the trustee signed consent orders to dismiss the March 2017 proceedings and provided these to the Court. The Court formally dismissed the proceedings on 1 February 2018.

On 23 February 2018, Dr Nugawela appealed the Court's decision to dismiss the March 2017 proceedings.

Issues

- Were the proceedings abandoned by the trustee under s 60?
- Did the trustee have the power to consent to dismissal of the proceedings where the subject matter had no direct connection to the property being administered?
- Did Dr Nugawela have standing to appeal given his bankruptcy?

Reasoning

The Court found that the trustee had not made an election under s 60(2) within 28 days of the 21 July 2017 notice, and so the proceedings were deemed to be abandoned. However, abandonment does not automatically dismiss the underlying cause of action. Further, abandonment is not a bar to commencing fresh proceedings. Further, the Court held that the abandonment operated regardless of whether the subject matter of the March 2017 proceedings formed part of the bankrupt estate, as abandonment occurs by operation of law.

The Court held that the March 2017 proceedings were connected to the property of the bankrupt estate firstly because they related to the bankrupt's liability to pay tax. While the Court did not expand on this, presumably its reasoning was that tax liability affects the overall balance of assets and liabilities of the estate. It was also connected to the property of the estate because the proceedings could expose the estate to a costs order if they were eventually dismissed. Therefore, the trustee could consent to discontinue the proceedings.

It follows that Dr Nugawela did not have standing to bring the March 2017 proceedings or the appeal against their dismissal, because upon bankruptcy, his interest in them vested in his trustee.

Lastly, the Court noted that Dr Nugawela was not competent to challenge the DCT in regards to the making of the sequestration order. This is because it was not the DCT, but the Registrar of the Court that had made the sequestration order.

Decision

The appeal was dismissed. The Court ordered costs against Dr Nugawela in his personal capacity, so as not to unfairly have creditors of the bankrupt estate bear these costs.

Mallett v Inspector-General in Bankruptcy [2018] AATA 3739

Background

Ms Mallett became bankrupt by debtor's petition on 17 June 2014. Prior to bankruptcy, Ms Mallett was involved in family law divorce proceedings and was also liable for a $6.5m taxation debt. In the course of the family law proceedings, Ms Mallett sought legal advice on how best to protect her assets. She was advised to establish a family trust. She did so, gifting it $3.1m. Before bankruptcy, she spent the majority of this money to pay children's school fees, legal costs, accounting costs and general children's expenses. At the date of bankruptcy, there was around $14,000 remaining.

Her (registered) trustee filed an objection to her discharge on three grounds:

1. A gift of $3.1m to a family trust she controlled was void under s 121 – s 149D(1)(ab).
2. Failure to adequately explain the purpose for money spent – s 149D(1)(g)(i).
3. Failure to comply with a request for written information about property/income – s 149D(1)(d).

Ms Mallett asked the Inspector-General in Bankruptcy (IG) to review the trustee's notice of objection under s 149K. The IG upheld the objection, confirming ground 1 and cancelling grounds 2 and 3. Ms Mallett asked the Administrative Appeals Tribunal (AAT) to review the decision of the IG.

Issues

1. Did the $3.1m gift to the family trust constitute a void transfer under s 121?
2. To be void under s 121, is the trustee required to take positive steps to call for the delivery or revesting of the funds?

Reasoning

Ground 1 – s 121 void transfer of $3.1m

The Court held that the ground was properly specified in the trustee's notice of objection, even though it referred only to the $3.1m gift and not to the $14,000 remaining in the account upon bankruptcy. It was clear the $14,000 was part of the $3.1m, so it didn't need to be specified in the notice.

The requirement that the purpose of the transfer was to avoid creditors (s 121(1)(b)(i)) was satisfied. This was because the legal advice stated that the purpose was 'to prevent claims by third parties'. The broad nature of this advice satisfied the purpose requirement, even though the bankrupt was not specifically seeking advice on avoiding creditors in insolvency. Further, applying s 121(2) in the context (where she had a $6.5m tax debt on foot as well as the family law proceedings), it could be inferred she was insolvent.

However, the AAT held that the transfer of the $3.1m (minus the $14,000) would probably not have become part of the bankrupt estate because the funds would have been expended in any event—that is, whether or not she had set up the trust. However, the remaining $14,000 was held to satisfy the requirements of s 121(1).

Lastly, the AAT held, applying *Re Cummins and Westpac v Bell Group* (2012) 44 WAR 1, that s 121 does not require the trustee to have taken positive steps to call for the money to be delivered or revested in the bankrupt estate. Therefore, even though the trustee had not raised the $3.1m gift before it lodged its notice of objection, it was still 'void'; 'all that is necessary is for a transaction to satisfy the criteria of section 121' ([48]). The tribunal stated that 'void' means 'voidable', in the sense that voidable means the transaction stands until positive action is taken to void it. However, the trustee's actions are not relevant as an element of s 121; i.e. the court can declare that a transaction is void notwithstanding the trustee has not attempted to get the money back. On the other hand, it is relevant (applying *Official Trustee in Bankruptcy v Alvaro* (1996) FCR 372) at the later stage when the trustee is seeking relief from the third party to whom the transfer was made.

Grounds 2 and 3

The IG had decided Ms Mallett had a reasonable excuse for failing to comply, and the AAT affirmed this decision. The AAT stressed the importance of giving warnings when requesting information/explanations from bankrupts. In this case, the trustee had not given any warnings to the bankrupt that if she did not comply with requests, explanations/written information, there was a possibility her bankruptcy could be extended. Therefore, Ms Mallett had a reasonable excuse for failing to comply.

Decision

Given a s 121 void transfer was made out, and Ms Mallett had no reasonable excuse for her conduct (s149N(1A)(c)), the AAT found Ground 1 was upheld and affirmed the IG's decision to not cancel the objection to discharge.

Meg Wootten
Legal Officer — Legal and Governance

Income contribution assessments under section 139Y of the Bankruptcy Act

Trustees have many powers under the *Bankruptcy Act 1966* (the Act), with respect to the basis and methods to assess a bankrupts' income contribution liability determination under the Act.

When determining a bankrupt's reasonable income under s139Y of the Act, the trustee must act prudently and reasonably and not in a manner which may be categorised as being arbitrarily, or capriciously, or in bad faith.

(1) Section 139Y: trustee may regard bankrupt as receiving reasonable remuneration.

Section 139X (1) of the *Bankruptcy Act 1966* (the Act) states that in making an assessment of the bankrupt's income during a contribution assessment period, the trustee may regard any information provided by the bankrupt or any other information in the trustee's possession.

In some instances, the trustee may disregard the information provided by the bankrupt under s 139X(2) of the Act and may make an assessment on the basis of what the trustee considers to be the correct information.

Alternatively, the trustee may deem the bankrupt's income pursuant to s 139Y of the Act.

- Section 139S of the Act sets out the formula to be used for determining the contribution payable by a bankrupt.
- Section 139Y of the Act sets out the conditions under which a trustee may regard a bankrupt as receiving or has received reasonable remuneration under certain circumstances.
- Section 139ZG of the Act sets out the circumstances under which contribution is payable.
- When determining the bankrupt's reasonable income under s 139Y of the Act, the trustee must act prudently and reasonably and not in a manner that may be categorised as being arbitrarily, or capriciously, or in bad faith.
- If the bankrupt's employment is subject to an award—or other industrial instrument—in order for the trustee to determine reasonable income of the bankrupt, the bankrupt must be receiving either:

    a. no remuneration for that employment or
    b. less than the amount that might be expected to be received for that employment under the award or instrument (reasonable remuneration).

What would be considered reasonable income?

Deputy President McMahon in *Re: Nelson and Inspector-General of Bankruptcy* (1994) 35 ALD 113, made the following helpful observations when considering the operations of s 139Y.

> *'Section 139Y (1) (b) draws a distinction between what might reasonably be expected to be or to have been received by "a person" in subpara (ii).The second paragraph therefore does not necessarily refer to the bankrupt but refers to a hypothetical person engaged in similar employment, work or activities in an arm length situation. In my view, however, it is necessary to pay some regard to the particular circumstances of the bankrupt in order that the expectation can be seen to be reasonable.'* (pages 117–118)

There are two relevant elements to be considered by the trustees in assessing the bankrupt's reasonable income under this section:

a. the bankrupt is engaged in employment or other work activities that resemble employment or work **and**
b. the bankrupt did not receive any remuneration or received less than what the provision identifies as reasonable remuneration.

In considering the above two elements, the following factors should also be taken into consideration as part of the trustee's decision in arriving at the bankrupt's reasonable income under s 139Y of the Act for contribution assessment purposes:

- bankrupt's employment history before and after the date of bankruptcy
- personal circumstances of the bankrupt such as physical health, age and also any adverse impact that may have had on his or her employment opportunities as a result of being an undischarged bankrupt
- whether or not the remuneration received by the bankrupt was on an arm length basis and/or commensurate with the bankrupt's level of skill and experience employed for the relevant tasks he or she has undertaken
- the bankrupt's skills and work undertaken prior to the bankruptcy may be considered as a measure of the skills and experience possessed and whether they were being employed during the period of the bankruptcy (*Pattison v Schiffer* [2007] FMCA 319 at [59] (O'Dwyer FM).

(2) Whether to allow income tax deduction when deeming income of a bankrupt.

Section 139N (1) (i) of the Act states that the income that is likely to be derived or was derived, by a bankrupt during a contribution assessment period, is taken to be reduced by any amount that the bankrupt pays or likely to be liable to pay, or paid or was liable to pay—as the case may be—during that period in respect of income tax (but not including any amount that is in respect of a provable debt).

However, it should be noted that when income contribution assessments are made under s 139Y of the Act (i.e. on deemed reasonable income basis), no income tax payable relevant to the deemed income should be allowed as a deduction from the income in calculating the bankrupt's contribution liability.

This is so because at the date of the assessment, the bankrupt would not have paid or was liable to pay any income tax on the deemed component of the income and as such, no deduction allowance should be made pursuant to s 139N (1) (i) of the Act.

This is the method adopted by O'Dwyer FM in the matter of *Pattison v Schiffer* [2007] FMCA 319 (16 March 2007), who having earlier noted that in calculating the amount of the contribution required to be paid, no allowance was made by the applicant for any deemed income tax payable on that amount of $74,665. Then after observing that had there been an allowance made for deemed tax payable on that amount then the contribution sought by the applicant would be considerably lower [32], concluded that:

> *'At the time the assessment was made, because it was an assessment of reasonable income and because the*

applicant was of the reasonable belief that no tax would be paid, he was justified in not deducting any amount for deemed income tax as his duty to the creditors was to gain a contribution from the assessed disposable income of the respondent, and not disadvantage the creditors by giving, in effect, a credit and benefit to the respondent for deemed tax.' (paragraph 69)

Paul Devellerez
Assistant Director, Technical — Regulation

AFSA intervenes in composition proposal

AFSA regularly attends meetings of creditors to monitor compliance with legislation, intervening where necessary to address deficiencies or to provide guidance to trustees.

Recent issues we have identified include inadequate investigation or inadequate reporting of material issues prior to meetings being held, such as the debtor's involvement in related entities or equitable interest in property.

Consequently, creditors may then be unable to consider these details when deciding whether to accept proposals.

In one example, a bankrupt sought to use related entity funds to put forward a s 73 composition proposal to creditors. This related entity was considered to be insolvent, and a transfer of funds out of the company may later be subject to recovery as a voidable or uncommercial transaction under the *Corporations Act 2001*. AFSA raised this issue with the trustee and subsequently a new source of funds was utilised in an amended proposal.

Section 12(4) of the *Bankruptcy Act 1966* was amended by the *Insolvency Law Reform Act 2016*, and gives the Inspector-General in Bankruptcy (IG) power to disclose information obtained through its functions to other Commonwealth entities and professional disciplinary bodies. Where issues of concern are identified, the IG will consider whether these fall within the scope of other agencies (such as the Australian Securities and Investments Commission) and will facilitate a co-regulatory approach to address these.

Melissa Frost
Senior Inspector — Regulation

Australian Taxation Office update

Australian Government
Australian Taxation Office

Keep up to date with what's happening at the Australian Taxation Office (ATO), including proof and voting entitlements for superannuation guarantee charge.

Proof and voting entitlements for superannuation guarantee charge

Employers must make superannuation contributions for their employees on a quarterly basis within 28 days of the end of each quarter. Superannuation contributions not paid on time and in full automatically become part of a superannuation guarantee charge (SGC). The SGC is equivalent to the amount of the unpaid superannuation contributions, plus an interest component and an administrative charge.

The SGC is classified as a tax-related liability and represents a debt due to the Commonwealth. The Commissioner of Taxation (the Commissioner) acts as agent of the Commonwealth in collection of the SGC. Following collection, the Commissioner redistributes the shortfall component and the interest component to the employees' respective

superannuation funds.

Insolvency practitioners are reminded that:

- the Commissioner is the only person entitled to prove for SGC in either a corporate or a personal insolvency administration
- neither the former employee nor his or her superannuation fund is authorised to lodge a proof of debt in relation to SGC, or vote at a creditors meeting in relation to any SGC debt
- neither the former employee nor his or her superannuation fund may rely upon an SGC debt to qualify themselves as a creditor eligible to serve on a committee of inspection.

More information

If you would like to find out more about using the ATO Business Portal, managing access or our education visits, please email your contact details to InsolvencyPractitionerServices@ato.gov.au

For general information, refer to the insolvency practitioners section on ato.gov.au/insolvency

Bronwyn du Mont, Director
Debt—Significant Debt Management, Australian Taxation Office

Recent prosecutions

- NSW (Fizelle) – Bankrupt convicted for disposing of money before becoming bankrupt
- SA (Vadasz) – Bankrupt piling contractor guilty of obtaining credit without disclosing bankruptcy
- SA (Donaldson) – Bankrupt man made false declarations and disposed of shares worth $86,000
- Qld (Page) – Ex-bankrupt pleads guilty to concealing boat and obtaining goods and services without disclosing bankruptcy
- SA (Schifilliti) – Bankrupt convicted for obtaining loan without disclosing his bankruptcy
- NSW (Khalsa) – Midwife sentenced for bankruptcy offences
- Qld (Johns) – Bankrupt convicted for failing to file a statement of affairs form
- NSW (Hatzipetros) – Bankrupt convicted of failing to provide information to trustee
- Vic (Leeder) – Bankrupt convicted for removal of property prior to bankruptcy and disposal of property with intention to defraud

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