



THE BANKRUPTCY REGULATOR

Volume 2 Issue 1

January 2003

This client newsletter by ITSA's Bankruptcy Regulation branch will be issued each quarter to registered and controlling trustees. In keeping with one of Bankruptcy Regulation's main purposes it is aimed at informing bankruptcy trustees of changes to bankruptcy law, both legislative and case law, and discussing areas of practice and Inspector-General requirements. Articles are welcome and can be forwarded by email to br.qld@itsa.gov.au

BANKRUPTCY LAW

BLAB passes both houses

The *Bankruptcy Legislation Amendment Act 2002* received Royal Assent on 18 December 2002. The changes made by that Act will commence on a date fixed by Proclamation. The intention is that the changes will commence on 5 May 2003.

As a reminder, the most important changes made by this Act are as follows.

(1) New power to reject debtor's petitions

An Official Receiver will be able to reject a debtor's petition where it appears that, within a reasonable time, the debtor could pay all the debts listed in their statement of affairs and that the debtor's petition is an abuse of the bankruptcy system. For the petition to amount to an abuse of the bankruptcy system, one of the following conditions must be satisfied:

- a) it appears that the debtor is unwilling to pay one or more debts to a particular creditor or creditors or is unwilling to pay creditors in general; or
- b) before the current petition was presented, the debtor had been bankrupt on a debtor's petition at least three times or at least once in the past five years.

The discretion can only be exercised in these circumstances and the change does not introduce an insolvency test. ITSA is developing a Best Practice Statement which will explain how this discretion will be exercised.

This change will apply only to debtors' petitions presented on or after 5 May 2003.

(2) Remove early discharge

Bankrupts will no longer be able to apply for early discharge from bankruptcy. This will apply to bankruptcies where the date of bankruptcy is on or after 5 May 2003.

This change will address the perception that bankruptcy has become too easy and will encourage debtors in financial difficulty to consider alternatives to bankruptcy. Early discharge has become the most common reason for people being dissatisfied with the bankruptcy system.

(3) Objections to discharge easier to uphold

The Act changes the requirements for objecting to a bankrupt's discharge. Where the ground for lodging an objection relates to uncooperative conduct by the bankrupt (one of the 'special grounds' listed in the Act), the trustee will not have to provide a reason for lodging an objection. Previously, the trustee always had to provide reasons and this was the most common reason for objections being overturned by the Inspector-General or the Administrative Appeals Tribunal.

These amendments are aimed at encouraging the bankrupt to cooperate fully with the trustee.

These changes will apply to existing bankruptcies but only to objections filed on or after 5 May 2003.

(4) Increase the income cut off for Part IX debt agreements

The Act increases by 50% the income cut-off for debt agreements so that more people who are able to make special arrangements to repay debts can enter debt agreements. This means the income threshold will be about \$48000 after tax. The new threshold will apply to debt agreement proposals made on or after 5 May 2003.

(5) Inspector-General's powers

The Inspector-General will have the power to make inquiries into and regulate the activities of debt agreement administrators and solicitors who act as controlling trustees. These powers will be covered in Regulations made under the Act. The Regulations have not yet been drafted but are likely to cover matters such as disclosure of fees to creditors and eligibility to perform these functions.

The Inspector-General's investigative powers will apply to conduct which occurs on or after 5 May 2003.

(6) Streamlining

The Act makes a number of changes aimed at streamlining many administrative processes required by the Act. These changes should reduce the cost of administering a bankrupt estate.

ITSA intends to run a series of information sessions for practitioners to explain these changes in more detail. We expect these sessions to take place in March and April.

Included Inside This Issue

- 1 BLAB passes both houses
- 2 Sticking PINS in the right place
- 3 Recent Case Law
- 4 GST Refunds
- 5 In the AAT
- 7 Section 237A Certificates

Sticking PINS in the Right Place

In recent times there has been both comments and questions raised by practitioners and their legal advisers over the weight and standing of the Personal Insolvency National Standards (PINS).

In 1996 the IPAA and ITSA agreed to jointly develop and implement national standards of personal insolvency administration. It is worthy repeating in this article the joint Inspector-General and IPAA communiqué that accompanied their release:

“The expected outcomes from the establishment and implementation of national standards are:

- *to ensure that personal insolvency administrations are maintained at a consistently high level by the Official Trustee and registered trustees*
- *to ensure that a level playing field applies to the regulation of all trustees, both the Official Trustee and registered trustees, by applying agreed national standards*
- *to increase the confidence of clients and stakeholders as to the level of consistency in the application of bankruptcy law and practice*
- *to encourage the identification and application of best practice in estate administration to the work conducted by all trustees*

The elements included in each standard are; timeliness, decision making, documentation and ethical practices and conduct.

Where the term “debtor” is used in a standard, the standard has application to both bankruptcy and Part X matters. For those standards which apply specifically to a bankruptcy, the word “bankrupt” is used in the standard.”

As intended, Bankruptcy Regulation is using these agreed industry standards as the benchmark by which it is assessing performance of bankruptcy trustees.

Registered Trustees who either continually fail to comply with the accepted standards, or whose failure to comply has a serious impact on an administration, can expect to be called to explain before a disciplinary committee who will determine whether their registration should be cancelled.

The fact that the PINS are not embodied in the Act or Regulations does not detract from their importance as the accepted industry standard. Any Court of review would give similar weight to their

importance when considering whether a trustee's conduct has been of an acceptable standard.

BR together with ITSA's trustee arm and the IPAA are about to commence a review of the PINS with a view to incorporating the BLAA, strengthening the Part X standards for Controlling Trustees and reinforcing the ethics and conduct expected by the IPAA within PINS.

Recent Case Law

“As safe as houses?”

O'Brien v Sheahan [2002] FCA (21 October 2002)

On 21 October 2002, Justice Carr in the Federal Court applied the doctrine of equitable estoppel to prevent a bankruptcy trustee from selling vested property and ordered that the property be transferred back to the bankrupts, after discharge.

Mr and Mrs O'Brien became bankrupt on 5 November 1996 and at that date there was no equity in the jointly owned matrimonial property. In the 5 years after bankruptcy the bankrupts had maintained mortgage and other related payments and substantial equity in the property had arisen.

Whilst no express statement was made by the original trustee that the bankrupts could keep the property, his honour determined that the conduct of both trustees was such that they had impliedly represented to the bankrupts that the trustees did not propose to assert any entitlement to any net proceeds from the realisation of the property and that this had been to the bankrupts detriment by their making mortgage and rates payments and carrying out substantial renovations.

The case provides a factual example of the circumstances in which equitable estoppel can apply. Trustees should take the time to read the case and consider whether there is any need to change the procedures currently employed when dealing with property with little or no apparent equity.

BR understands that consideration is being given to lodging an appeal against the decision and will keep you updated should this eventuate.

GST Refunds

There have been cases of late where some bankruptcy trustees have misinterpreted the GST legislation when administering a bankruptcy or Part X matter and have inappropriately claimed GST refunds either in non business administrations or in respect to non business related costs incurred.

Generally, bankruptcy trustees are only required to submit Business Activity Statements (BAS) as representatives of incapacitated entities, that is, as trustee of a specific Bankruptcy Act administration, if the bankrupt or debtor operated business activities.

Most trustees operate their own businesses as insolvency practitioners and are required in that separate activity to submit BAS's. This fact however is not relevant to the issue of whether they need to submit an administration based BAS and does not entitle a trustee to claim GST refunds in non business related bankruptcies or Part X matters.

In addition, GST debits only apply to **business related** sales (taxable supplies) and input tax credits are only claimable if they relate to **business related** costs (creditable acquisitions) incurred in selling business assets or running a bankrupt's or debtor's business enterprise.

Input tax credits are not claimable **at the estate level** on administration costs that are not connected to the bankrupt's or debtor's business activity.

If we consider trustee's remuneration by way of example, whilst a trustee is required to submit their practice BAS and pay GST on fees earned less any input tax credits, this does not entitle a trustee to lodge an estate BAS to claim the remuneration paid out of the estate as a creditable acquisition, to which an input credit applies, **unless** the work undertaken by the trustee relates to selling of business related assets or business related activity in the estate.

Where there is a mix of business assets and non business assets, the ATO requires a trustee to apportion their costs between the two. For a registered trustee, a time based apportionment is appropriate.

Hence in non business related estates or where costs are incurred not associated with estate business related activity, the estate, through the trustee, is effectively an end user (i.e. is input taxed) and bears the GST component factored into costs incurred in the estate with no right to claim an input tax credit.

If you are in any doubt the ATO through their Tax Practitioners Industry Partnership (TPIP) have set up an insolvency GST Referral team to assist trustees and they can be contacted at ATO Canberra (02) 621 62869.

In addition many questions and answers on GST are available through the TPIP website at:

<http://www.taxreform.ato.gov.au/content.asp?doc=/content/15803.htm>

In the AAT

This article is provided as a reference for trustees who may find themselves in the AAT for a review of their decision or a review of an Inspector-General decision. Unless otherwise stated sections referred to relate to the AAT Act.

1. INTRODUCTION

Since 1 July 1992 the Administrative Appeals Tribunal (AAT) has been a review tribunal for Bankruptcy legislation decisions in the areas of contributions, early discharges and objections to automatic discharge.

A bankrupt can make application to the AAT directly to review a trustee decision or if they have firstly been subject to an Inspector-General Review then either a bankrupt or trustee can make application to the AAT to review an Inspector-General review of the primary decision.

2. TIME LIMITS

a) Applications

An application to the AAT should be made within 28 days of the day on which the decision is given to the applicant, (section 29(2)). The application is to be in writing and on the prescribed form available from the AAT. If an application is out of time, the respondent will be asked if they have any objection to an extension being granted. The AAT has the power to grant an extension under s. 29(7).

b) "T Documents"

The person who has made a decision (respondent), subject to an application for review by the AAT is required to lodge with the AAT, within 28 days after receiving the notice of the application, 2 copies of the "T documents".

3. T DOCUMENTS

The T documents are to include:

- a s37 statement setting out the findings on material questions of fact, referring to the

evidence on which those findings were based and giving the reasons for the decision;

- every other document that is considered by the decision maker to be relevant to the review.

When preparing the "T documents" it is recommended that the index is prepared first, this approach assists in logically putting together the documentation and helps to ensure that documents and evidence are not overlooked. The first document will be the application for review, the second will be the respondents s 37 statement and the remaining documents will be arranged in date order from the earliest to the latest.

The decision subject to appeal is to be included and is to be underlined in the index. Relevant legislation is to be included at the end of the documentation.



4. APPLICATION TO STAY

The AAT Act provides the power under s. 41(2) to stay or otherwise affect the implementation of a decision before the application for review is heard.

However this power will not be used as the AAT has found that the Bankruptcy Act takes precedence over the AAT Act. Specifically in respect to Contribution assessment reviews the AAT found section 139ZG of the Bankruptcy Act (BA) must be given some work to do and that it was implied that s139ZG(2) of the BA was inserted to repeal the powers of the AAT.

5. PRELIMINARY CONFERENCE

A preliminary conference ("PC") will usually be set down 6 weeks after the "T documents" have been filed. A member of the AAT will chair the PC which can either be held in person or over the telephone and this will depend on where the applicant is located.

The PC is without prejudice and the member sitting will not be involved in the hearing, if the administrative review proceeds that far. The purpose of the PC is to identify and clarify the issues and to ascertain if any "common ground" can be established. The PC's are informal with all persons being able to have a say if they wish. If common ground can be established and the

matter can be resolved at the PC then a hearing will not be necessary, otherwise the matter will proceed to a hearing.

If issues require further investigation prior to the hearing, then a second PC may be set down.

It is important to establish at the PC and indeed at the hearing, that the respondent is only trying to establish the truth in order that the correct decision is made and that the respondent has a duty to the creditors of the bankrupt estate. It is an inappropriate use of the AAT and its powers as a tactical exercise or to use PC's or a hearing as a "fishing expedition".

6. HEARING

a) General

The AAT is usually made up of 3 members. Each district AAT has Deputy Presidents, Senior Members and Members.

The AAT hearing is a "merits review", that is, the facts up to and including the hearing will be considered by the AAT. The original decision maker and the review officer may have had certain facts available to them at the time of making their decision and made it accordingly, however by the time the case is heard by the AAT, other facts may have been made available by the applicant which may alter the original decision. The overall goal is to obtain the truth and a correct decision in accordance with the Bankruptcy Legislation.

b) Presentation of case

The "T documents" are tendered at the start of the hearing as an exhibit for the respondent.

If the applicant is represented it is usual practice that their representative will commence the hearing with an opening address. This opening will identify the issues and the appropriate legislation that is to be applied. If witnesses are to be called they will be identified at this time.

If the applicant is unrepresented, the respondent's representative will open the hearing.

c) Evidence -general

Section 33(1)(c) provides that the AAT is not bound by the rules of evidence but may inform

PRACTICE

itself on any matter in such manner as it thinks appropriate.

Evidence will include the “T documents”; written reports, for example reports from real estate agents and accountants; other documents such as reference books and books of account; evidence from witnesses in the form of sworn statements; and oral evidence from witnesses either in person or by telephone (obviously prior arrangements will need to be made with the AAT and the witness in these circumstances).

It is very important to establish the credibility of any witnesses to be called prior to the hearing. The case could turn on this factor.

d) Order of evidence

The applicant usually gives evidence first and will then be cross-examined on that evidence by the respondent. If there are any matters requiring clarification by the AAT they will then question the applicant.

The applicant’s witnesses will then be called and the same procedure followed.

The respondent will then call their witnesses. Cross-examination by the applicant and questioning by the AAT will also take place if necessary.

e) Final address

The respondent commences the final address first with a right of reply at the end. The final address is to bring together the case and highlight the discrepancies in the other party’s case. The relevant legislation and cases are also cited at this point and are applied to the facts of the case in issue.

7. DECISIONS

The AAT may give an oral or written decision.

The AAT is the final arbitrator of fact, therefore it is important to ensure that all facts relevant to the case are available, including any witnesses and any documentation prior to the commencement of the hearing.

The AAT will also give guidance in relation to the interpretation of the law; however appeals on a point of law may be made to the Federal Court of Australia.

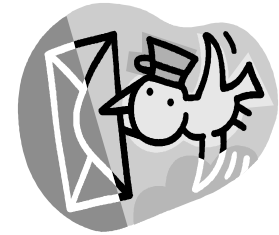
Annette Moodie
Director Southern Region

**Section 237A
Certificates**

Bankruptcy Regulation have noted of late that some trustees appear to be of the misunderstanding that in Deeds of Arrangement, a s 237A certificate by the trustee “that provisions of the deed have been carried out” can only be issued once a final dividend has been paid.

Whilst this requirement exists in relation to Deeds of Assignment under section 232, the Act does not impose a similar requirement in respect to Deeds of Arrangement. BR are of the opinion that once the debtor has fulfilled their obligations under a Deed of Arrangement, a certificate can be issued, without having to wait for the payment of a final dividend.

How to Contact us:



<p>Queensland and South Australia</p> <p>Arthur Carrick tel 07-3360 5404 Robert Tom tel 07 3360 5406 Charles Smith tel 07 3360 5425 Greg Barrett tel 07 3360 5425</p>	<p>PO Box 10443, Adelaide St BRISBANE QLD 4000 Facsimile: (07) 3360 5466 Email br.qld@itsa.gov.au</p>
<p>New South Wales</p> <p>Mike Barr tel 02-8233 7873 Mark Findlay tel 02 8233 7860 Helen Karalemas tel 02 8233 7802 Adrian Jones tel 02 8233 7857</p>	<p>Level 8, 135 King Street Sydney NSW 2000 Facsimile: 02-8233 7805 Email: br.nsw@itsa.gov.au</p>
<p>Victoria and Tasmania</p> <p>Annette Moodie tel 03 9272 4805 Anthony Chow tel 03 9272 4915 Terry Clarke tel 03 9272 4891 John Kennedy tel 03 9272 4886 Paul Noonan tel 03 9272 4918</p>	<p>Level 10, Melbourne Central 360 Elizabeth Street MELBOURNE VIC 3000 Facsimile: (03) 9272 4940 Email br.vic@itsa.gov.au</p>
<p>Western Australia</p> <p>Athena Burton tel 08 9268 1204</p>	<p>GPO Box H536 PERTH WA 6001 Facsimile: (08) 9268 1218 Email br.wa@itsa.gov.au</p>
<p>National Manager</p> <p>Andrew Robinson tel 07 3360 5405</p>	<p>PO Box 10443, Adelaide St BRISBANE QLD 4000 Facsimile: (07) 3360 5466 Email br.qld@itsa.gov.au</p>