COVID-19: WILL ALL BUSINESSES GET THROUGH THIS? HOW? THE AUSTRALIAN EDITION

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Australian Competition Law Alert

By: Ian Dorey, Alex Smith, James W. Thompson

It is clear that there are going to be incredible impacts to businesses and companies of all sizes as a result of the COVID-19 pandemic. No business will be immune to the impact of this health epidemic. Across the globe, governments have responded in various ways to change insolvency laws in an attempt to provide assistance to those businesses affected directly or indirectly by COVID-19. Australia is no different and the Federal and State Governments have responded quickly to the crisis.

On 23 March 2020, we published an alert in response to the Federal Government's temporary changes to insolvency laws that were announced on 22 March 2020. In this article, we consider in greater depth the temporary changes to the insolvent trading regime in Australia, as well as considering the relief available to borrowers from the banking sector and to tenants in respect of their obligations to commercial landlords.

CHANGES TO INSOLVENCY LAWS

The changes we referred to in our earlier alert have since been embodied in the *Coronavirus Economic Response Package Omnibus Act 2020* (Cth) (*Response Act*) that included a number of amendments to the *Corporations Act 2001* (Cth) (*CA*) as well as the *Bankruptcy Act 1966* (Cth) (*BA*) as part of its assistance package.

Insolvent Trading

With one of the most stringent insolvent trading regimes in the world, it is not surprising that one of the announcements that the Federal government has made is a temporary "softening" of these laws. The changes have been effected by introducing a new section 588GAAA into the CA. During the six month period from 25 March 2020 (and any extension of that period if it is so prescribed), directors will be relieved from their duty to prevent a company from trading whilst insolvent with respect to debts incurred in the ordinary course of carrying on its business prior to any administrator or liquidator being appointed.

What do These Changes Mean for Directors?

It follows that directors will not become personally liable for such debts as would normally be the case under the pre-COVID-19 insolvent trading regime in the event that the company is ultimately wound up. It is hoped that these changes will encourage directors to continue to trade, to the extent practically possible, during this time of extraordinary uncertainty we find ourselves in.

To avail themselves of the relief, directors will need to be satisfied that the debts are being incurred in the ordinary course of the company's business and will bear the onus of being able to prove that, if later required.

What Should Directors do Now?

In order to best protect their personal positions, and consistent with good corporate practice, directors would be well advised to document the basis upon which they decide that the company should continue to trade and incur liabilities notwithstanding its insolvency.

Boards should be meeting regularly (by telephone or other means consistent with required social distancing protocols) and documenting their company's survival plans. As well as incorporating an operational plan for the temporary shutdown or skeleton operational period, that survival plan should address the budget and revised cashflow forecast for the expected shutdown period, including factoring in the impact of any government relief and other accommodation afforded by, or agreed by negotiation with, financiers, landlords and key suppliers.

Now is the time for directors to communicate clearly and open up early negotiations with their key stakeholders to garner support for their plans.
In addition, the survival plan should note the anticipated sources of any restart capital that is forecast to be required to get the business back on its feet after the downtime, which is likely to require modelling and forecasting based on different assumed scenarios. There will likely be a significant overlap between this survival plan and the type of restructuring plan that would be required for the purpose of the pre-existing safe harbour relief contained in section 588GA of the CA, which relief remains available in parallel with the emergency temporary relief.

Unlike the temporary measures introduced in the UK, the Australian temporary relief does not have retrospective effect and does not apply to liability for debts incurred prior to 25 March 2020. Some prospect of relief may still exist for debts incurred prior to 25 March 2020 under the existing defences available by reason of section 588H of the CA or by relief from liability under section 1317S of the CA where the court is satisfied that the director acted honestly and ought fairly to be excused from liability.

The changes do not give directors relief from personal liability for company debts that are incurred when a company is insolvent and where dishonesty is involved, as the dishonesty offence under section 588G(3) of the CA will continue to apply unchanged.

Temporary Increase in Thresholds and Time to Comply

For both personal and corporate insolvency matters, the government is providing a temporary increase to the debt amount required to issue a Statutory Demand against a company and a Bankruptcy Notice against an individual. The government is also increasing the time within which a company and an individual has to comply with a Statutory Demand and a Bankruptcy Notice, respectively. Set out below are the new temporary changes:

- Statutory Demand threshold increased to A$20,000 (from A$2,000) and time to comply changed to 6 months (from 21 days)
- Bankruptcy Notice - threshold increased to A$20,000 (from A$5,000) and time to comply changed to 6 months (from 21 days).

The government has said that the changes set out above will apply for 6 months from 25 March 2020.

BANKS' RESPONSE TO COVID-19

Whilst many Australian banks have suffered adverse publicity as part of the fallout from the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, the major Australian banks have responded to the current crisis by providing assistance for businesses and individuals affected by COVID-19.

The business relief offered focusses on small business customers, which are considered to be some of the hardest hit by COVID-19, however, the Banks have extended some relief to businesses with business loan facilities of up to A$10 million.

While the specific relief offered varies to some extent between each bank, the general assistance offering includes:

- deferral of loan repayments for up to 6 months, with interest to be capitalised for both business and home loans;
- reduction in interest rates across both business and home loans;
- unsecured business loans of up to A$250,000 with no establishment or account fees and no repayments for 6 months. These facilities are offered as part of the Federal Government's Coronavirus SME Guarantee Scheme pursuant to which the Federal Government will guarantee up to 50% of the value of the loan;
- refunding late fees and interest charges on credit cards; and
- commercial landlords with loan facilities up to A$10 million can obtain relief subject to providing an undertaking not to evict tenants due to their inability to pay rent as a result of the COVID-19 pandemic.

For most of the relief offered, bank customers will need to establish that they have in fact been financially impacted by COVID-19. The level of "proof" that is required varies across the financial institutions and will seek to prevent the relief being abused by those who are not genuinely struggling as a result of the COVID-19 pandemic.

However, these eligibility limitations do not apply to all of the relief offerings. For example, while applicants will have to meet the relevant bank's credit assessment criteria, the offer of unsecured business loans of up to A$250,000 does not appear to be restricted to COVID-19 affected customers.

A question also arises as to what will happen at the end of the deferrals referred to above. While borrowers will generally have the option to either repay the additional loan amount over the existing life of the loan, or look to extend the term, it appears unlikely that 6 months will be a sufficient amount of time for the economy to recover and borrowers to 'get back on their feet'. While the relief being offered by the Banks is welcome, it may yet prove to be not enough for borrowers to weather the impact of the pandemic.

LANDLORDS AND TENANTS - WHAT HAPPENS HERE?

On 29 March 2020, the National Cabinet agreed to a 6 month moratorium on evictions for residential and commercial tenants that have been affected by coronavirus.

On 7 April 2020, the National Cabinet further agreed to implement a mandatory Code of Conduct (*Code of Conduct*) for commercial tenancies where the tenant is a small-medium enterprise (annual turnover of up to A$50 million) and is an eligible business for the Commonwealth Government's JobKeeper programme (*Eligible Tenants*). The Code of Conduct is intended "*to aid the management of cashflow for SME tenants and landlords on*

a proportionate basis" and will apply to "*all tenancies that are suffering financial stress or hardship as a result of the COVID-19 pandemic*", where the tenant is an Eligible Tenant. Notably, the Code of Conduct does not apply to residential tenancies.

Tenancy laws in Australia, both commercial and residential, are governed by the States and the Code of Conduct is "*to be given effect through relevant state and territory legislation or regulation as appropriate*". Various States have started to implement changes to their legislation around commercial and residential tenancies, although more is needed to legislate the Code of Conduct with respect to commercial tenancies in all of the States.

CONCLUSION

The Federal and State Governments are to be commended for the (generally) cohesive way they are working together to assist businesses and individuals in this time of global turmoil. The Australian banks are also doing their bit to alleviate some of the pain being suffered by their customers. However, there is no doubt that there will unfortunately be significant economic fallout from the effects of travel restrictions and social distancing in connection with the COVID-19 pandemic.

For small businesses, which historically have been and will continue to be an important part of the Australian economy, now is the time to make use of the assistance packages created by the Federal Government as well as the other tools previously put in place, such as Safe Harbour protection, to formulate a plan and act on it.

KEY CONTACTS

IAN DOREY
PARTNER

BRISBANE
+61.7.3233.1236
IAN.DOREY@KLGATES.COM

ALEX SMITH
PARTNER

SYDNEY
+61.2.9513.2434
ALEX.SMITH@KLGATES.COM

