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FEG Policy Team

Department of Employment and Workplace Relations

Dear Department

Consultation on addressing corporate misuse of the Fair Entitlements Guarantee

Thank you for the opportunity to comment on the discussion paper *Addressing corporate misuse of the Fair Entitlements Guarantee* (**FEG**)(**Discussion Paper**).

The Australian Institute of Company Directors' (**AICD**) mission is to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society. The AICD's membership of more than 53,000 reflects the diversity of Australia's director community, comprised of directors and leaders of not-for-profits (**NFPs**), large and small and medium enterprises (**SMEs**) and the government sector.

The AICD has in recent years engaged extensively on Government insolvency reforms, including the introduction of the insolvency safe harbour (**Safe Harbour**), the statutory review of the safe harbour (**Safe Harbour Review**) and the Parliamentary Joint Committee on Corporations and Financial Services inquiry into corporate insolvency in Australia in 2022 (**PJC Inquiry**).[1] We also participated in consultation in 2018 on measures to strengthen the integrity of the FEG contained in *Corporations Amendment (Strengthening Protections for Employee Entitlements) Bill 2018*, which ultimately passed the Parliament in 2019.[2]

This submission is informed by engagement with AICD members, insolvency professionals and industry bodies and is limited to the questions on director accountability.

1. Executive Summary

The AICD strongly supports the operation of the FEG as a scheme of last resort that ensures that employees are paid their entitlements in the event of the insolvency of their employer. We also recognise that the FEG must operate in a sustainable way to ensure it is available for genuine claims into the future.

The Discussion Paper details concerns that the FEG is being misused by 'sharp corporate practices' through a small subset of business owners, directors and advisers deliberately taking action to avoid the payment of employee entitlements. This is resulting in a growing reliance on the FEG.

The AICD supports greater regulator prioritisation and resourcing of FEG misuse as a key mechanism to ensure the FEG remains viable. However, as detailed in this submission the AICD does not support any changes to existing director accountability mechanisms. To tinker with these already punitive settings

[1] AICD submission to PJC Inquiry, November 2022, available here.

[2] AICD submission on Exposure Draft *Corporations Amendment (Strengthening Protections for Employees Entitlements) Bill 2018*, July 2018, available here.

would further heighten Australia's risk averse and compliance focused corporate governance culture and do little to reduce sharp corporate practices.

Our key points are:

- The AICD strongly supports a comprehensive review of Australia's insolvency regime as was recommended by the PJC Inquiry in 2023. We are concerned that further material changes to the FEG would represent a continuation of the piecemeal nature of policy making in this critical area. We recommend that significant reform of the FEG is postponed until an independent comprehensive review can be completed.

- We urge greater prioritisation and resourcing by the Australian Securities and Investments Commission (**ASIC**) and the Australian Taxation Office (**ATO**) of the enforcement of existing legislative provisions relevant to the FEG, including phoenix activity. Regulators should be first looking to exercise their existing powers to combat this activity and send a deterrent signal to perpetrators, including directors, rather than seeking further complex law reform that will likely result in minimal benefits in reducing FEG misuse.

- We strongly support proactive and innovative steps to build awareness amongst directors of their duties and options available to turnaround financially struggling businesses. Providing directors, particularly of small businesses, with knowledge of their obligations and options for assistance may have a material impact on the number of businesses that enter liquidation and ultimately call on the FEG for the payment of employee entitlements.

- We do not support amendments to the FEG related director disqualification provisions in the *Corporations Act 2001* (**Corporations Act**) under sections 206EAB and 206GAA. Our strong view is that ASIC and the ATO should be utilising existing enforcement powers, including the current director disqualification provisions, to deter sharp corporate practices rather than further law reform.

- We do not support any changes to the existing personal liability settings on directors. Adding new or expanded avenues for personal liability associated with reliance on FEG will do nothing to disincentivise sharp corporate practices. It would also run the real risk of further stifling Australia's overly compliance focused corporate governance environment to the detriment of productivity and economic growth – two areas where Australia faces critical challenges.

2. Overarching policy comments

We make the following overarching policy comments on the case for amendments to the FEG legislative framework and alternatives to addressing sharp corporate practices.

a) Comprehensive review

The AICD is concerned that the proposals in the consultation paper to address the sustainability of the FEG represent a continuation of the 'piecemeal' approach to insolvency reform in Australia. This was identified by the PJC in its final report as contributing to the complexity, cost and inaccessibility of Australia's overall insolvency framework. These findings informed the PJC's recommendation for an independent comprehensive review of Australia's insolvency framework.[3]

In our submission to the PJC we strongly supported the necessity of a comprehensive 'root and branch' review.[4] Based on feedback from members our view was that the ad hoc and disjointed manner of reform over recent years has contributed to an insolvency regime that is increasingly complex and

[3] PJC, Final Report, pages 52 – 53.

[4] AICD submission, PJC Inquiry: Corporate Insolvency in Australia, November 2022, available here.

challenging for directors, advisors and regulators to navigate and oversee. In this context we note that the FEG was last reformed in 2019. The Discussion Paper is proposing a new round of material changes that are addressing the same policy concerns that were the basis of the 2018/19 consultation. It is not clear from the Discussion Paper whether the sustainability of the FEG has further deteriorated since 2018 and/or the Department has reached the view that those reforms have not been effective.

A comprehensive review would allow consideration of the effectiveness of the FEG, including director accountability settings, within the overall operation of the Australia's insolvency regime. Notably, our strong view is the case for changes to director liability and disqualification provisions in the Corporations Act, as is proposed in this consultation, should be assessed within the broader context of director duties, including the duty to prevent insolvent trading.

We recommend that significant reform of the FEG be postponed until an independent comprehensive review of Australia's insolvency regime can be completed.

b) Regulator enforcement of existing laws

The Discussion Paper is silent on enhancing or prioritising the enforcement of existing provisions that are intended to combat FEG misuse. Rather, the starting point of the Discussion Paper is that further law reform is required rather than a stronger focus on enforcing current laws. Our strong view is that regulators should be first looking to exercise their existing powers to combat this activity and send a deterrent signal to perpetrators, including directors, rather than seeking further complex law reform that will likely result in minimal benefits in reducing FEG misuse.

As noted above, we share the concerns of the Government with misuse of the FEG through sharp corporate practices, including phoenix activity. However, we note recent public commentary that ASIC and the ATO have taken limited public enforcement activity, including disqualifying directors, relative to the estimated size of the problem.[5] Further, as discussed below, ASIC has not once disqualified a director due an association with repeated FEG access.

We recommend greater prioritisation by both ASIC and ATO for enforcement activity associated with phoenix activity, asset shifting and broader sharp corporate practices that impact the sustainability of the FEG. Further, this should be supported with greater funding for liquidator investigations through the FEG Recovery Program.

c) Director awareness building

The AICD strongly supports any steps to build awareness amongst directors of their duties and options available to turnaround financially struggling businesses. We consider that a proactive and innovative approach to equipping directors, particularly of small businesses, with knowledge of their obligations and options for assistance may result in less businesses entering liquidation behind on employee entitlements and with minimal assets.

Our sense is that many directors of small businesses have a limited understanding of their directors' duties, including the insolvent trading duty, and the potential liability or penalties associated with breaches. For instance, we suspect that many directors starting a business may not be aware of severity of the ATO's Direct Penalty Notice powers. We also consider that there is likely limited awareness of the options available to directors when a business faces financial difficulties.

The Safe Harbour Review found that the Safe Harbour has been an effective reform in providing an option for directors of large financial struggling businesses to focus on turnaround options, rather than

[5] Australian Financial Review, 'Easy money': regulators lax on a scam that costs the economy $5b a year', 28 February 2025.

prematurely putting a business into administration.[6] Further, the increasing uptake of the Small Business Restructuring (**SBR**) regime points to the demand from directors, and their advisors, to proactively work through financial challenges. A precondition of access to both the Safe Harbour and the SBR is the business is up-to-date with its employee entitlements.

The apparent success of these reforms indicates that when there is sufficient awareness that many directors, supported by professional advice, will take steps to turnaround financially challenged businesses.

The AICD includes information on the insolvency regime in our education courses, director tools and regularly provides updates to members on changes.[7] However, while the AICD has a large membership base it is only a fraction of the number of directors in Australia, many of whom will be resource constrained to undertake formal education or professional development.

We would therefore strongly support greater awareness building by the ATO and ASIC to reach directors and their advisors. For instance, ASIC recently updated *RG 217 Duty to prevent insolvent trading* to contain information on the Safe Harbour, despite the reform commencing in 2017. While this delayed update is welcome, RG 217 is still dense and complex guidance that is targeted at advisers. We are not aware of any proactive steps by ASIC or the ATO to reach directors, particularly of small businesses, to explain their duties.

An awareness building strategy will not reduce premediated and egregious sharp corporate practices however it may still have a material impact on the number of businesses that enter liquidation and ultimately call on the FEG for the payment of employee entitlements.

3. Director accountability

This section responds to questions 10 and 11 on director disqualification and director personal liability.

a) Director disqualification

The AICD does not support amendments to the FEG related director disqualification provisions in the Corporations Act under sections 206EAB and 206GAA.

We are concerned that the policy case for strengthening these provisions is that ASIC has not utilised them to date to bring one disqualification. While it is not stated, it appears the subtext for this proposal is that they have not been used by ASIC as the barriers to utilising them are too high. A proposed legislative change that goes to personal liability should be supported by a strong policy rationale and robust cost benefit analysis. In this case we would expect detail on ASIC's attempts to utilise existing provisions, why these attempts have failed and how a legislative change would result in policy benefits, such as increased deterrence of sharp corporate practices.

Further, we are concerned with the legal implications of the proposal to remove the existing threshold that the individual was a director of the company (or within 12 months) at the time the company began to be wound up. The practical result of such a change is a director could be disqualified if at any point over seven years two companies they were a director of were wound up and relied on the FEG. This could occur even when the director is long removed from holding an officer position with a company and did not participate, or have any knowledge, of the actions of the company immediately prior to being wound up. Our view is that is in direct conflict with the fundamental legal principle that an

[6] The Treasury, Review of the insolvent trading safe harbour - Final report, March 2022.

[7] AICD member article, *Insolvency trends, updated ASIC guidance and the Small Business Restructuring Regime: What Directors Need to Know*, March 2025, available here.

individual can only be held personally liable for their own actions, participation or involvement in a wrongful act.

As discussed above, our strong view is that ASIC and the ATO should be utilising existing enforcement powers, including director disqualification, to deter sharp corporate practices. We are not satisfied based on the very limited information in the Discussion Paper that amending the disqualification provisions is necessary or a legally sound policy proposal.

b) Director personal liability for employee entitlements in insolvency

The AICD strongly opposes any changes to the existing personal liability settings on directors. Adding new or expanded avenues for personal liability will do nothing to disincentivise sharp corporate practices. It would also run the real risk of further stifling Australia's already overly compliance focused corporate governance environment to the detriment of productivity and economic growth.

As noted in the Discussion Paper, directors can be held personally liable for unpaid employee entitlements through a range of mechanisms, notably under section 550 of the *Fair Work Act 2009* and separately section 596ACA of the Corporations Act. Separately, the ATO has very extensive administrative powers to issue a director penalty notice (**DPN**) for the non-payment of employee superannuation entitlements. While changes to the DPN regime is not within scope of this consultation it is a very powerful administrative tool, particularly lockdown DPNs, that is at the disposal of the ATO to incentivise directors to be up-to-date with employee entitlements.

These avenues for personal liability of directors informed the conclusion by Allens Linklaters in 2020 that Australia's insolvency regime is amongst the strictest in the world.[8] This analysis, prepared for the AICD, found that Australia's insolvent trading laws take a punitive approach through both the potential for criminal and civil liability, which is out of step with settings in the United Kingdom, New Zealand, Hong Kong, Canada and the United States.

To contemplate adding new or expanded forms of personal liability would be a regressive policy step that would be inconsistent with the objectives of the Safe Harbour and the SBR regimes that are designed to free directors from the straitjacket of liability and actively seek to turnaround struggling businesses.

As discussed above, we strongly recommend that to address misconduct by directors engaging in sharp corporate practices that ASIC and the ATO should prioritise investigations and utilising existing laws.

Next Steps

We hope our submission will be of assistance. If you would like to discuss any aspects further, please contact Simon Mitchell, Senior Policy Adviser at smitchell@aicd.com.au or Christian Gergis, Head of Policy at cgergis@aicd.com.au.

Yours sincerely,

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[8] AICD research, *Criminal and Civil Frameworks for Imposing Liability on Directors*, February 2020, available here.