SAFE HARBOUR

A Fresh Start Begins Here
How does Safe Harbour apply to my business should it get into trouble.

The term ‘safe harbour’ provides some protections for directors against the statutory duty to prevent a company trading while insolvent.

Australian insolvency laws have been reviewed, resulting in changes to include safe harbour provisions providing directors with restructuring options before moving into formal insolvency. Previously insolvency laws do not typically offer pathways for businesses to restructure. As a result, insolvency laws are viewed as counterproductive in allowing directors the time and opportunity to make critical changes so that companies can find solutions to trade successfully.

The main aim is to provide options for directors to restructure so that the business can continue to trade rather than moving straight into voluntary administration or liquidation. The Safe Harbour legislation has been designed to improve formal insolvency processes and provide a pathway for businesses to be successful.
The reforms also aim to encourage a culture for businesses to restructure and act early as a first option before entering into a traditional insolvency process. Directors will opt for insolvency to avoid tough penalties that continue to trade a company while it is insolvent.

Typically directors move their companies straight into voluntary administration or liquidation as the penalties levied on directors are viewed as harsh while trading insolvent.

Such is the concern around penalties; directors will appoint an insolvency practitioner to the company at the expense of exploring viable restructuring options. Safe Harbour is a tool now available to Directors that should be explored with your insolvency practitioner to see if it is a viable option to allow the business to be restructured.
Understanding Insolvent Trading and how it applies to directors

The Corporations Act 2001 section 588G enforces a duty on directors to prevent a company from incurring a debt(s) when the director has reasonable grounds to suspect it cannot pay its debts as and when they fall due. A trading company that is insolvent and a director allows the company to incur new debt; then, the director can be personally liable for the new debts incurred.

Although some defences are available to a director, liability for insolvent trading under Australian insolvency laws can expose a director to a range of penalties, including civil or criminal penalty orders or orders for compensation to creditors who suffered loss. Consequently, insolvent trading claims can expose directors to bankruptcy and loss of personal assets if they do not have the financial capacity to satisfy any monetary judgment entered against them.

A liquidator has the right to issue an insolvent trading claim on a director without having to attend court.
How can Safe Harbour Provisions Assist Directors:

The threat of Australia’s insolvent trading laws, combined with uncertainty over the precise moment a company becomes insolvent, has long been the main driving force of directors to seek voluntary administration. As opposed to exploring restructuring opportunities where the company may be viable in the longer term, which would benefit all parties.

Australia’s Insolvency Laws creates the following environment:

- Discourage directors to innovate, make changes and take risks that will result in the company trading out of financial challenges.
- Insolvency laws typically penalise failure even when the director may have acted openly and in good faith.
- Greatly reduce the company’s value when a voluntary administrator is appointed before opportunities can be explored to restructure the business and trade on.
- Companies being placed into liquidation can result in loss of confidence of stakeholders in the business following the appointment of an administrator.
How Safe Harbour can provide better outcomes for all parties:

The amendments give directors a safe harbour from civil insolvent trading provisions contained in section 588G of the Corporations Act. Should the requirements be satisfied, this provision allows directors the opportunity to restructure or turnaround the business.

The safe harbour provisions apply, provided the requirements are satisfied according to the conditions set in section 588G. Once the director starts to suspect the company is or may become insolvent, the director must begin to develop a course(s) of action that can reasonably lead to better outcomes for the company. The endorsed safe harbour provision is activated from when the director starts to develop strategies to set a pathway out of insolvency.

For the directors to utilise the safe harbour provisions, the responsibility is on the directors to demonstrate that they have implemented the following actions:

- The directors have been taking appropriate steps to develop or implement a plan to restructure the company to improve its financial position:
- The Directors have adopted a course of action that is likely to lead to better financial outcomes for the company:
- The directors have maintained up to date financial reporting so they can remain informed about the company’s financial position:
- The directors have taken steps to prevent misconduct by employees of the company:
- The directors have engaged appropriate advice from a qualified adviser or insolvency firm.
The company must comply with its obligations to pay its employees and employee entitlements, including their superannuation. In addition, all tax reporting obligations must be satisfied.

The director(s) must comply with formal obligations should the company be unable to be turned around if the company is placed into formal insolvency.

Safe Harbour applies from the time the director suspects the company may become insolvent and starts to adopt safe Harbour to the time they stop complying with the safe harbour requirements.

Safe Harbour will also limit the compensation payable by a holding company where the directors benefited from Safe Harbour.
How tph Advisory Can Help

Safe Harbour is now available to provide the time and space to restructure and turn around the business. tph provides a systematic step-by-step approach to the implementation of Safe Harbour, which simultaneously meets the legislative requirements of Safe Harbour while also maximising the chances of a successful turnaround and continued operation. This system meets but goes beyond the guidelines provided by the Turnaround Management Association.

The tph Advisory system includes cash flow analysis, debt negotiation, short-term cashflow resolution, strategic direction, personnel management, KPI management, sales and marketing, accounting and bookkeeping systems and services and more.

The road map for business out of covid and the government support will come to an end. It is now up to business and the economy to perform. The government has not prescribed how business should get back to trading; this ultimately is up to each business. The government has retained some limiting conditions until at least the 1st of December 2021.

We think now is the time that SME’s should be looking to their trusted financial advisors to help develop a way forward for business that is losing government subsidies. However, we also think that some of these businesses will struggle initially and unless they can have protection from trading insolvently, the recovery may well be short-lived.

Advisors should have a solid understanding of the safe harbour regime as that is a potential lifeline that can provide a type of insurance policy if things don’t work out.

Contact tph Advisory for a free, confidential consultation to discuss how acting early can help turnaround and restructure your business using Safe Harbour.

1300 756 425 or enquiry@tphadvisory.com.au
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