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Insolvent Trading

“Am I in Breach?”

BACKGROUND

A constant question that is raised by Directors during consultations when discussing those various options available the Companies experiencing difficulties, is are they breaching those Insolvent Trading Provisions of the Corporations Act and if so what are the consequences.

The response is that the answer lies within and is very much subjective ie:

CORPORATIONS ACT 2001 - SECT 588G

Director's duty to prevent insolvent trading by company

(1) This section applies if:

(a) a person is a director of a company at the time when the company incurs a debt; and

(b) the company is insolvent at that time, or becomes insolvent by incurring that debt, or by incurring at that time debts including that debt; and

(c) at that time, there are reasonable grounds for suspecting that the company is insolvent, or would so become insolvent, as the case may be

In summary it is a “reasonable man” test in that should an alternate party be faced with the same decision would they under the circumstances have incurred that debt and other debts at the time and would the Company remain as a consequence solvent.

There are though several fatal and non-rebuttable circumstances that will in effect deny a Director any defence to an Insolvent Trading claim and they are:

- Failure to maintain proper Books & Records within the ambit of Section 286 of the Act for at least the period in question, and
- Failure to service the Company’s Statutory obligations in respect to servicing of its BAS and SGC obligations

CONSEQUENCES

Section 588M of the Act avails a Liquidator or a Creditor (with the Liquidators consent) the power to issue for recovery the amount equal to the loss or damage arising from Insolvent Trading.

Any such breach also falls within the strict liability provisions of the Act and can see a Director issued with a Pecuniary Penalty Order of up to \$200,000.

CONCLUSION

In summary it is well worth your client ensuring they are seeking and obtaining timely financial advice as to the affairs of their Company to ensure if things were to go awry then those “reasonable man” defences may be available.

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