



ARITA
AUSTRALIAN RESTRUCTURING
INSOLVENCY & TURNAROUND
ASSOCIATION

Safe harbour guidance for ARITA Members

What is safe harbour?

'Safe harbour' is protection for company directors from liability for insolvent trading in the event that the company goes into liquidation.

Safe harbour is not:

- a type of appointment under the *Corporations Act*
- a state that a company operates in, or
- something that directors can resolve that the company enters into.

The protection arises due to the steps that the directors' take prior to liquidation as part of an attempted turnaround or restructure.

Advising directors about safe harbour protection

The safe harbour laws commenced on 19 September 2017 and open opportunities for directors to turn around their financially distressed company without risking personal liability under Australia's insolvent trading laws.

The important thing to remember is that there are very strict rules around when the safe harbour protection is available to directors. As an advisor engaged by the director, it is important that you ensure that they are aware of these rules.

- The safe harbour protection from liability for insolvent trading once a company is in liquidation is only available to directors who:
 - developed or took a course of action that, at the time, was reasonably likely to lead to a better outcome for the company than

immediate administration or liquidation (the course of action that was developed must have been implemented within a reasonable period)

- ensured that the company complied with its obligation to pay its employees (including their superannuation),
 - ensured that the company met its tax reporting obligations; and
 - met their obligations to assist administrators, liquidators or controllers and provide them with the company's books and records and Report as to Affairs once the company entered external administration.
- The safe harbour only extends to debts incurred directly or indirectly in connection with the course of action or its development.

The reasonably likely to lead to a better outcome test

- The law provides a list of indicative factors to be considered in determining whether a course of action was reasonably likely to lead to a better outcome. These factors are whether the director has:
 - kept themselves informed about the company's financial position
 - taken steps to prevent misconduct by officers and employees of the company that could adversely affect the company's ability to pay all its debts

- taken appropriate steps to ensure the company maintained appropriate financial records
- obtained advice from an appropriately qualified adviser, and
- been taking appropriate steps to develop or implement a plan to restructure the company to improve its financial position.
- Whether a course of action is reasonably likely to lead to a better outcome is assessed at the time the decision is made, not with the benefit of hindsight.
- The benefits of safe harbour can also extend to a holding company where the directors of the subsidiary had the benefit of safe harbour and the holding company was taking reasonable steps to ensure that this was the case.
- A director seeking to claim the benefit of the safe harbour bears the evidentiary burden of establishing that:
 - he or she developed a course of action that was reasonably likely to lead to a better outcome for the company; and
 - the debt was incurred directly or in connection with the course of action.
- It will then be up to the liquidator to show, on the balance of probabilities, that the course of action taken was not, at the time, reasonably likely to lead to a better outcome.

Ongoing director obligations

- The protection provided to directors by the safe harbour is limited to civil liability under the insolvent trading provisions. Directors must continue to comply with all of their other legal obligations and duties.

- Continuous disclosure requirements, if applicable, continue to apply.
- If the restructuring plan were to fail and the company entered liquidation, the safe harbour will only protect directors from a liquidator's insolvent trading claim if the directors comply with certain formal obligations during the liquidation, such as completing a ROCAP and providing books and records. These would generally include records of the restructuring attempts undertaken, including the documentation of the better outcome assessment.
- A director that fails to provide access to books and records to a liquidator or administrator will be prevented from being able to rely on those materials as evidence of having complied with the safe harbour requirements – but the liquidator or administrator must ensure they advise the directors of this consequence when making the request.

Documenting the engagement

The terms of the engagement and basis of remuneration should be documented and agreed with the client. As restructuring plans should be flexible, advisors should ensure that engagement letters are regularly updated to reflect any material changes to scope.

Advice should be provided in writing. This will assist the directors to support their claim for safe harbour protection if the restructuring fails and a liquidator is appointed.

In the event of the appointment of a liquidator or voluntary administrator, you should co-operate with the appointee and provide any relevant requested information about the restructuring and your engagement.

Formal insolvent appointments following a safe harbour engagement

There will be situations where a formal appointment will occur notwithstanding restructuring attempts. For example, the attempted restructure of the business may be unsuccessful and the company may need to be placed into liquidation, or a voluntary administration may be required as part of the restructure.

A request to take an appointment following an engagement as an adviser to a company will be subject to the same independence rules as any other prior professional relationship with the company.

The fact that the engagement is part of the director's strategy to enjoy safe harbour protection in the event of failure of the restructuring plan makes no difference to the independence considerations that apply.

As stated in the Code, a Practitioner must be and must be seen to be independent. That is, they must not accept an appointment if:

- a reasonable and informed third party
- on the information available (or which should have been available) at the time
- might reasonably form the opinion that the Practitioner might not bring an independent mind to the administration and thus may not be impartial or may in fact act with bias
- because of a lack of independence, or a perception of a lack of independence.

The 'two-year rule' and the exceptions to that rule are also relevant. Consideration can be given to whether the engagement was an immaterial professional relationship, pre-appointment communications and meetings, or an investigating accountant leading to an appointment.

Independence example

If you were approached to act as an adviser in a restructuring plan and at your first meeting with the directors, before you provide any advice, you assess that a restructure is highly unlikely and you recommend that the company enter into voluntary administration, you would be able to take the appointment as this would fit within the 'pre-appointment communications and meetings' exception.

However, if after two months of acting as the company's adviser and providing advice to the board, it became apparent that the restructure is not working and the company has to enter into voluntary administration or liquidation, you would be unable to take the appointment as you have a prior professional relationship with the company that does not fit within one of the exceptions.

An administrator or liquidator requesting books and records or access to books and records must include in the notice to the directors the consequences of failing to comply with the request, namely that the directors will be unable to rely on those materials as evidence of having complied with the safe harbour requirements unless they are provided in accordance with the request. An administrator or liquidator that fails to do so will not be able to use non-compliance with the request to challenge the operation of the safe harbour.