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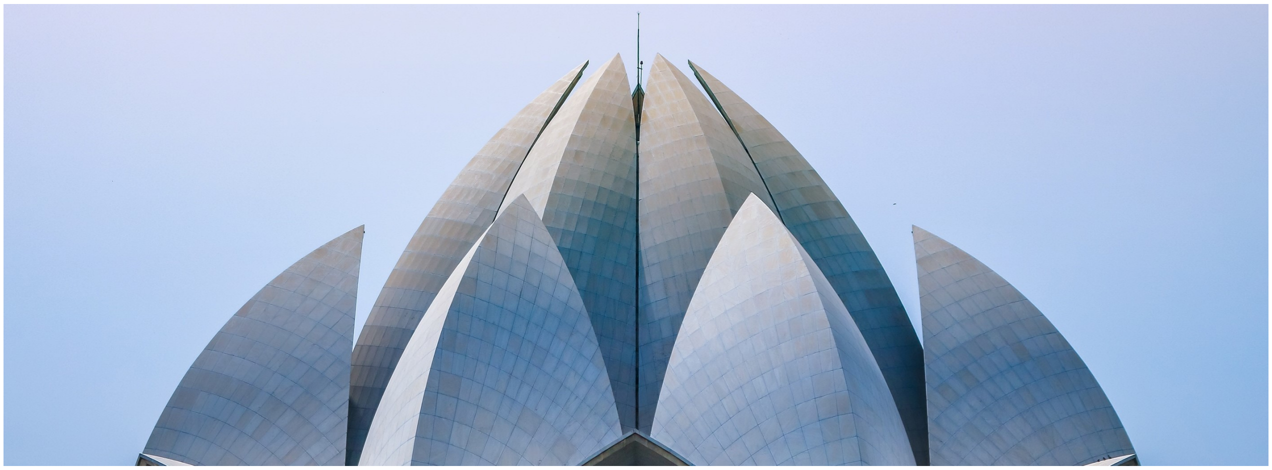

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# PHOENIX ACTIVITY: WHEN LEGALITY TURNS MURKY

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## WHAT IS ILLEGAL PHOENIX ACTIVITY?

Kreisson is often asked by trade suppliers, professional consultants and subcontractors in the building and construction industry to help recover unpaid debts from ‘phoenix’ operators.

Illegal phoenix activity involves the creation of a new company to take over an existing business for often less than market value. After it has been stripped of its assets, the business is liquidated. Its ultimate owners are not held responsible for unpaid debts, taxes and employee entitlements.

The construction industry has a greater credit risk from insolvencies than any other industry–- it accounts for 20-25% of all insolvencies in Australia even though it generates less than 10% of GDP.

Illegal phoenix activity hurts suppliers and employees. *The Economic Impact of Potential Illegal Phoenix Activity Report*[1] found that in 2015, employees lost $298 million in unpaid entitlements. In the same year, the government lost around $1,660 million in unpaid taxes which directly hurts the broader community.

Phoenix activity is not in of itself illegal. Criminality hinges on the intent motivating the activity.

Federal legislation prohibits company directors and officers from disposing of a company’s assets with the intention of:

- realising less than the best price reasonably obtainable under prevailing market conditions;
- putting assets beyond the reach of creditors or hindering or delaying their realisation in winding-up; and
- evading proper winding-up processes.

The ASIC website notes that:

*"Not all company failures will involve illegal phoenix activity. Genuine company failures do occur. Where a business has been responsibly managed, but fails, that business may continue after liquidation by using another corporate entity without, necessarily, being involved in illegal phoenix activity."* [2]

## WHAT ARE THE WARNING SIGNS OF PHOENIX ACTIVITY?

Insolvency practitioners and their lawyers are routinely asked to investigate suspected phoenix activity. Corporations should always be on the lookout for indicators like:

- the debtor's name is changed to match its Australian Company Number;
- business documents show a slight change of name and different A.B.N;
- an ASIC search shows that ABN is held by a new incorporated company;
- the ASIC search shows the new company is run by close relatives of the debtor's directors;
- payment and payment cycles are made from different bank accounts;
- petty objections are raised to delay payment of invoices; and
- customers are asked to redirect payments elsewhere.

## WHAT CAN BE DONE?

Liquidators and creditors can require the return or restoration of assets that have been stripped from a company. Alternatively, they can seek monetary compensation for the lost value. The corporate regulator also has significant powers to combat criminal phoenix activity.

ASIC actively identifies directors who are repeatedly involved in failed companies. It uses data analytics, conducts surveillance and subsidises liquidators to detect phoenix activity.

## KEY TAKEAWAYS

- The prevalence of illegal phoenix activity is expected to rise in the wake of the economic climate impacted by COVID-19.
- Business' should implement precautioning measures to detect suspected phoenix activity.
- It is easier to undertake preventative measures to ensure invoices are paid than to recover assets in insolvency.

Call us early for help collecting the debts justly to you. Our commercially astute lawyers have the knowledge and experience to recover assets that have been stripped from a company.

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## REFERENCES


1. *The Economic Impact of Potential Illegal Phoenix Activity Report* (2018)

2. *Media Release: https://www.ato.gov.au/uploadedFiles/Content/ITX/downloads/The_economic_impacts_of_potential_illegal_Phoenix_activity.pdf*


## CONTACT US


If you would like assistance or further information regarding phoenix activity, please contact Kreisson on *(02) 8239 6500* or at *excellence@kreisson.com.au*.