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Ruling boosts insolvency law

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Receivers don't have to pay full entitlements to staff they retain as soon as they take over failing companies, according to a court ruling that is likely to encourage firms to trade out of trouble and banks to lend more freely.

The Federal Court decision is a relief to insolvency practitioners who claim that an alternative ruling would have produced a windfall for workers.

An alternative ruling would also have made it harder for companies to trade out of difficulties.

It is the first time the court has clarified the position of employees in a receivership.

The ruling gives Australia's insolvency regulations more credibility at a time when many larger corporations begin to question openly the need for Chapter 11-style provisions in the Corporations Act.

Experts claim the decision this month is a boon for small businesses as banks will be encouraged to reduce lending restrictions if they know that non-performing borrowers can be more readily traded as continuing concerns during hard times.

The court ruled that the receiver for Tasmanian shipbuilder Incat Tasmania Pty Ltd was not obliged to pay annual leave, long-service leave or retrenchment entitlements to

employees who were retained in the business after his appointment.

A lawyer for Incat, Steven Palmer, finance services partner at Deacons, said that if the decision had gone the other way, receivers would be forced to pay out all entitlements and retrenchment costs to employees, even those who still worked for the company, threatening the ability of the business to trade out of difficulty.

"The decision gives comfort to financiers, both at lending and enforcement stages, as businesses

"The court has clarified the position of employees in a receivership."

will be able to continue to trade upon the appointment of a receiver without the negative impact on working capital, which would result from the need to actually pay long-service leave and annual leave to employees whose employment continues," he said.

Incat was placed into receivership in March last year with total liabilities of \$100 million — \$70 million owed to the National Australia Bank and \$30 million to the Tasmanian government — after not selling a vessel since October 2000.

David McEvoy, receiver for Incat, shed some of the workforce

upon his appointment but maintained a majority of staff in an attempt to trade out of the receivership.

Mr McEvoy sought direction from the court on the priority of payments to employees after the non-terminated workforce argued they were eligible for all annual leave, long-service leave and retrenchment entitlements.

The workers claimed that under the Corporations Act they should be treated in the same manner of the sacked workers and be deemed to have been terminated upon the appointment of the receiver.

This would make them eligible for their entitlements and retrenchment pay as a priority payment despite the fact they still had a job with the company.

In his judgement, Justice Ray Finkelstein described as "absurd" the interpretation of the law that would result in a worker keeping a job and being paid out as if that job had been lost.

"A construction which places employees of a company in receivership on the same footing as employees of a company which has been wound up will operate in a discriminatory fashion, as the former employees will both keep their jobs and be paid out as if they had lost them," he said.

Mark Mentha, principal of Korda Mentha and administrator of Ansett, said the decision confirmed the superiority of Australia's insolvency laws.