

# News with Clout

Providing Corporate & Personal Solvency Solutions

## **IPSO FACTO AFFECT ON INSOLVENCY TO BE LIMITED**

At the risk of sensationalizing something a tad mundane this article is about laws coming into effect that will make ipso facto clauses in contracts of no effect in certain insolvency situations.

From reading the explanatory memorandum to parliament the idea of this legislation is to address the effect of clauses in contracts that terminate the agreement automatically on the occurrence of certain insolvency appointments despite a parties honouring of all the other terms of the agreement.

You may or may not recall that the introduction of the Voluntary Administration process in 1993 was after a horrendous period of economic disruption. Its purpose was enshrined in the legislation at Section 435A of the Corporations Act, to where possible save the Company or if not the Company then the business. This was a recognition that generally liquidation was an erosion of value for both creditors and members.

Two and a half decades later another bout of insolvencies and there is the realization that Voluntary Administration did not work either in this regard.

Enter the Safe Harbour procedure as one initiative and also the addressing of another reason for failure of the legislation being the automatic provisions terminating contracts, the ipso facto clauses. We are also aware that the current National Government is trying to foster innovation.

Our current legal environment is seen as an impediment to fostering venture capital and risk taking. Ipso facto clauses certainly help in the erosion of value but it is not certain that the fostering of innovation could really be the motivation behind this particular tranche of the amendments.

Clearly they saw the introduction of the Safe Harbour legislation was a convenient time to address this universal contractual problem.

To be specific this legislation is directed at clauses regularly found in contracts such as leases, supply agreements and licenses. Previously a formal appointment saw the tenancy terminated, supply agreements and license agreements pulled. Often with these gone there is little left.

Now a scheme of arrangement or the appointment of a Voluntary Administrator or a controller under a charge will stay the effect of ipso facto clauses unless an election is made by the appointor.

The stay remains in effect even after the appointment ceases or goes from an Administration to a Deed of Company Arrangement or even a liquidation. Unsurprisingly the stay does not apply to a straight appointment of a liquidator.

Any other terminating provisions such as nonpayment or nonperformance remain in effect.

The minister still needs to formulate regulations yet on which contracts to which this provision will not apply.

These provisions are due to kick in on the later of the 1<sup>st</sup> July 2018 or six months after Royal Assent or earlier if the Governor General so determines.

It appears it is only going to apply to arrangements or agreements entered into after this becomes law which is pretty disappointing as we feel it could well be a few years before the positive impacts of this legislation is felt in the insolvency arena. Still it is a move in the right direction.

As ever we welcome your enquiries.



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