

Illegal phoenix activity

Illegal phoenix activity occurs when a new company, for little or no value, continues the business of an existing company that has been liquidated or otherwise abandoned to avoid paying outstanding debts, which can include taxes, creditors and employee entitlements.

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What is illegal phoenix activity?

This illegal practice usually happens when company directors abandon the company or transfer the business of an existing company to a new company without paying true or market value, leaving debts with the old company. Once the assets have been transferred, the old company is placed in liquidation or abandoned. If the liquidator is appointed, there are no assets to recover, which means creditors cannot be paid.

Once the assets are transferred to a new company, the directors continue to operate the business. This gives the new business an unfair advantage when competing for work, because they have less debt and lower operating costs.

Illegal phoenix activity directly impacts sub-contractors, creditors and employees as they are left unpaid and out of pocket. It also indirectly impacts the broader community because the company avoids having to pay tax, while at the same time Government often has to subsidise outstanding employee entitlements of liquidated companies.

The [Economic Impact of Potential Illegal Phoenix Activity Report](#) found that illegal phoenix activity costs employees between \$31 and \$298 million in unpaid entitlements and costs the Government around \$1,660 million in unpaid taxes and compliance.

Penalties for illegal phoenix activity

Illegal phoenix activity can involve breaches of [directors' duties](#) (including [failing to prevent creditor-defeating dispositions](#)), fraudulent concealment or removal of assets and fraud by company officers under the *Corporations Act 2001*. Penalties include large fines and up to 15 years' imprisonment for company directors and secretaries.

Directors should be wary of dishonest advisers who approach financially distressed businesses and offer to help restructure a company, especially when that advice will enable the business to continue trading without having any debts. The advice may

inadvertently lead company directors to breach the law and engage in misconduct such as illegal phoenix activity.

Each person involved in the activity, including the pre-insolvency adviser, valuer, liquidator and dummy directors, may be subjected to the same penalties as a company director or secretary if they aided, abetted, counselled or procured a director to engage in illegal phoenix activity or creditor-defeating dispositions.

Warning signs of illegal phoenix activity

The warning signs of illegal phoenix activity can include:

- the company fails and cannot pay its debts
- the company changes its name to its Australian Company Number (ACN) and a new company is registered, often with a similar name to the old company
- the directors or former directors transfer the assets from the old company to the new company for less than market value
- the new company operates the same or similar business as the old company, sometimes from the same premises, using the same assets and employees
- the new company often uses the same bank account, advertising material, websites or contact details as the old company
- the people involved in managing the old company control the new company.

Find out what to do if you have [concerns about illegal phoenix activity](#).

Key people required to set up a phoenix company

Those usually involved in illegal phoenix can include:

- **Pre-insolvency adviser:** An untrustworthy adviser who encourages illegal phoenix activity, maintains a network of 'friendly' professionals and can cold-call companies in financial trouble to offer their services. The pre-insolvency industry is unregulated, and advisers have varying qualifications and experience.
- **Valuer:** A 'friendly' valuer, usually engaged by the pre-insolvency adviser to provide low valuations of the company's assets
- **Liquidator:** A 'friendly' liquidator, usually engaged by the pre-insolvency adviser who avoids their responsibilities by not investigating the affairs of the company, not recovering illegally removed assets or reporting their findings to ASIC and creditors.
- **Dummy directors:** Fake directors appointed to the old company, just prior to its failure and/or to the new company, however, they are not involved in the running of either company. These directors can be unknowingly appointed and may include relatives, friends or associates. They can be referred to as 'directors for hire' and may be appointed on the instructions of the pre-insolvency adviser or phoenix operator to disguise the real perpetrators.

- **Phoenix operators:** These are the people that ultimately benefit from engaging in illegal phoenix activity. Referred to as 'controlling minds', they may be directors on the register and sometimes conceal their involvement by appointing 'dummy directors'. They may engage the services of dishonest pre-insolvency advisers to help them carry out the illegal business restructure.

Video: Would you know if a phoenix operator was ripping you off?

Difference between illegal phoenix activity and a legal phoenix company

Not all company failures involve illegal phoenix activity, as genuine company failures do occur. Where a director has responsibly managed a company and it subsequently fails, they can operate the same business using another company without engaging in illegal phoenix activity. This is often referred to as a 'company restructure'.

A responsibly managed company means the director has complied with their legal obligations and acted in the best interest of the company and its creditors. When a company restructure involves transferring assets to a new company, acting responsibly could mean having the assets independently valued to determine their true market value and the new company pays that value. Where a company is a small business, directors may enter into a restructuring by appointing a restructuring practitioner.

If the old company is wound up, then creditors would not be disadvantaged because they would still have access to the proceeds from sale of assets. For example, if plant and equipment was independently valued and sold for \$100,000 to another company, neither the old company or its creditors would be disadvantaged because they would have \$100,000 in lieu of the plant and equipment.

The key difference between a legitimate phoenix business rescue and illegal phoenix activity is the director's dishonest intentions or recklessness. Where a director sets out to intentionally avoid paying debts and liabilities, by transferring assets to another company without paying the true market value, or is reckless as to creditor harm, then the conduct is illegal.

Case study: Joe tries to save his failing building company

Joe, the director of Sample Homes Pty Ltd building company, knew his business was in trouble. For six months he had been paying contractors late and had accrued \$60,000 in overdue payments. His costs had blown out on major projects and he was unable to pay his suppliers, contractors, employees, loans and taxes.

Joe sought advice from his accountant, Trevor, who said he needed to take urgent steps to stop the company collapsing. Trevor introduced Joe to Carlos, a pre-insolvency adviser who offered to restructure the business for \$40,000.

Carlos advised Joe to change the name of Sample Homes to its Australian Company Number and register a new company, naming it Sample Homes (Vic) Pty Ltd. He told Joe that registering a company that had a very similar name would not alert the building industry of a change. Joe questioned the legality of the restructure, but Carlos assured him it was fine.

Joe was appointed director of the new company. Carlos engaged an associate to value the assets of the old company for an amount well-below market value. Carlos prepared an Asset Sale Agreement to give the impression that Sample Homes (Vic) had purchased the assets legitimately. Carlos had Joe sign the Asset Sale Agreement on behalf of each company and advised him not to pay the amount stated in the Agreement.

Carlos then moved Sample Homes bank accounts, plant and equipment, project contracts and employees to the new company that operated as normal and kept the liabilities with Sample Homes.

Work continued on existing projects and employees were unaware that they were employed by another company.

With no assets left in Sample Homes and minimal records, Carlos arranged the appointment of a 'friendly' liquidator who conducted limited enquiries about the cause of the company's failure and lodged a basic report to ASIC advising there were no assets to recover that could be used to pay creditors. The liquidator then applied to have the company deregistered.

As Joe and Carlos dishonestly removed the assets of the company, and the liquidator did not investigate the disposal and recover the assets, there were no assets to sell and creditors, employees and the ATO had no means of being paid outstanding debts.

Contractors of Sample Homes who did not get paid complained to the ATO via the ATO [Tip-Off form](#) (Phone: 1800 060 062) as they suspected illegal phoenix activity. After an investigation by ASIC and the ATO, Joe was charged with breaching his director duties obligations under the Corporations Act and was imprisoned for two years. Carlos and the liquidator were also charged for breaching the director duty provisions and were imprisoned for two years for aiding and abetting the illegal phoenix activity.

Related links

- [Where to report illegal phoenix activity](#)
- [ASIC action on illegal phoenix activity](#)

- [Resigning or removing a company director](#)