Bargaining for Security: Lessons for Employees from the World of Corporate Finance

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The plight of employees who lose accrued entitlements when their corporate employers collapse is a matter of continuing political and industrial interest. After the National Textiles collapse in January 2000, the Howard government introduced the Employee Entitlements Support Scheme to provide a taxpayer-funded, minimum safety net to cushion employees from the worst effects of employer insolvency. Just prior to the 2001 federal election, a more generous General Employee Entitlement Redundancy Scheme was introduced. These are administrative solutions, susceptible to the fickle winds of political expediency. There have been many calls for longer term legislative solutions—through industry-wide or national insurance or guarantee-fund schemes. This article explores a further alternative: using existing long-standing commercial law principles and practices to bargain for security. If employee representatives were to examine the principles of corporate law, and adopt the practices of corporate financiers, they might bargain more effectively for better protection than may be offered long term by a welfare-based safety net.

An alarming problem

The plight of employees who stand to lose entitlements when companies collapse has become a regular item on evening current affairs programs. From October to December 2001, the picket lines of Ansett employees—owed an estimated $300–400 million in entitlements—filled our television screens. In May 2001, Australians watched while One-Tel employees rushed to the Australian Industrial Relations Commission to secure redundancy pay entitlements before receiving their pink slips. In January 2001, the *Sydney Morning Herald* covered the story of Electruck Pty Ltd, a transport company that went into receivership owing some 40 workers about $1.1 million.[1] In November 2000, the Steel Tank and Pipe group of companies made the news, also because about 60 employees stood to lose about $3.3 million in lost wages, annual and long service leave entitlements, and redundancy pay.[2] According to the Employee Entitlements Support Scheme Year One Activity Report (published on the Department of Employment Workplace Relations and Small Business web-site at http://www.dewrsb.gov.au/) employees of an alarming 333 companies benefited from the scheme in its first

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year of operation. No-one can say whether this represents a sudden increase in corporate collapses. Historical information is not available.[3] It may be that the spread of redundancy benefits in awards and agreements since the *Termination Change and Redundancy Case* (1984) 8 IR 34 has increased the average amount of entitlements owed to employees when their employment is terminated because their employer goes out of business. So, more impressive employee losses may have attracted media attention to an older, but less visible problem. Nevertheless, it is clear that the Australian community—and consequently its political leaders—are now (if belatedly) sensitive to the problem.

THE NATIONAL TEXTILES RESPONSE

The longest running and most significant story was the National Textiles collapse in January 2000. It wasn't the first. Before National Textiles, there were plenty of stories about miners and meatworkers losing their jobs and their entitlements.[4] National Textiles was the first, however, to invoke a sympathetic and practical response from the federal government. The fact that the collapse would create even further pressure on a depressed rural community in the Hunter region may have contributed to the response; or the fact that the textile industry generally had been suffering the effects of a program of tariff reductions. Whatever the particular reasons, the time was certainly ripe in January 2000 to give some serious attention to a problem that had been causing growing community concern. Three measures were introduced to address the problem:

1. A special bail-out for these particular workers (subject to all creditors agreeing to a scheme of arrangement).[5] (A government-managed bail-out, funded through airline ticket sales, was also introduced to fund Ansett workers' entitlements in late 2001.)
2. A new safety net scheme for all cases arising after January 2000. The Employee Entitlements Support Scheme (EESS) reported that in its first year of operation it paid more than $3 million to more than 1600 employees.[6] Following the Ansett collapse (which occurred during the run-up to the November 2001 federal election), this scheme was replaced with the more generous General Employee Entitlements Redundancy Scheme (GEERS).
3. A new Part 5.8A, 'Employee Entitlements', inserted into the Corporations Law,[7] to make company directors liable to compensate employees where they have entered into uncommercial transactions with the intention of avoiding payments to employees. (See Noakes (2001) for detailed discussion of the legislation.)

These measures have received a mixed reception from various sections of the Australian community, and there is still continuing debate about whether different or additional measures to address this problem are warranted. Ultimately, it may be that a legislated solution to this problem will be necessary. Both sides of politics, and many private groups, have investigated the feasibility of a special insurance scheme, similar to workers' compensation, or a compulsory savings fund scheme, similar to compulsory superannuation.[8] This paper, however, will leave consideration of these eminently sensible proposals to the insurance experts. While that debate continues (and may it ultimately bear useful fruit), this paper focuses on what employees might presently do, with the legal tools already available to the players in the commercial marketplace, to take some steps to solve this problem for themselves. Of course, not all employees presently enjoy the industrial muscle to wrest for themselves the legal advantages presently enjoyed by banks and professional service providers. There will always be a need for a welfare-based safety net, and this paper does not intend to denigrate in any way the EESS or the GEERS schemes as good starting points for solving this problem, especially for the most vulnerable in the working community. This paper has a simple agenda: it sets out, for the benefit of employee representatives interested in learning from commercial practice, how our system of private commercial law already protects certain classes of creditors, and how those legal tools might be adopted for the benefit of workers.

BARGAINED-FOR SOLUTIONS

Even the Minister, the Hon. Tony Abbott, conceded quite some time ago that 'the EESS is a safety net scheme, and does not preclude the adoption of additional measures by particular employers and employees' (Abbott 2001). This paper explores how additional security measures might be bargained for. Those measures need not involve outright contributions of actual dollars to trust funds or schemes. Banks take very effective security without extracting working capital from an enterprise. Employees should be able to use the same strategies that banks use. This paper aims to demonstrate some of the legal thinking that has presented obstacles in the past, and how those obstacles might be overcome.

First, however, we must acknowledge the steps already taken by the Australian Manufacturing Workers Union, who took the Minister at his word and mounted an extensive campaign to join employers up to ManuSafe, a self-funded, industry-wide long service and severance scheme.[9] This trust fund does envisage actual cash contributions by employers to a trustee, in respect of employee entitlements. Unfortunately, employers have not universally embraced the invitation to join this type of union-designed fund. Reasons include a general, ideologically-based mistrust of unions and their intentions for the new economic power that control of such a fund would confer, and specific criticisms of vagaries in the ManuSafe trust deed. For instance, the trust deed, in Clause 30.4, appears to confer considerable and apparently unfettered discretion on the trustee when it comes to deciding who should receive the benefit of forfeited benefits. Some of these criticisms are apparent in the dispute between Transfield and the Automotive, Food, Metals, Engineering, Printing and Kindred Industries Union. (See the decision of Justice Munro, Print PR908287, 30 August 2001, at paragraph 68.) This decision also provides a warning: claims for security for employee entitlements will need to be carefully framed so that they are clearly matters pertaining to the relationship between an employer *as employer* and employees *as employees*. A claim such as this, which was construed as a matter relating to a relationship between the employer as contributor to a fund, and a trustee, may be held to fall outside the legitimate subject matter for workplace bargaining. Action taken in support of such claims may not be protected action under section 170ML of the *Workplace Relations Act 1996* (Cwlth), and may not be safe from section 127 injunctions, ordering the action to cease (which was the result of Munro J's decision in the *Transfield* case). But this decision did leave scope for more carefully worded claims to succeed. (See paragraph 75.) This decision has also been called into doubt by the full Federal court decision in *Australian Worker's Union v Electolux Home Products Pty Ltd* [2002] FCAFC 199 (21 June 2002) which held that employees may not be able to obtain section 127 orders to stop industrial action, even if a matter is held not to be an 'industrial matter'. (The Electrolux decision is likely to be appealed.)

The AMWU has since been successful in negotiating security in the form of a bank guarantee of past and future entitlements in the Maintrain dispute.[10] It is this type of solution that this paper examines. That is, the prospect for employees, acting collectively, to take security comparable with the types of security taken by the finance creditors to their corporate employers. It is useful to examine the facts in the National Textiles case to demonstrate those features of our legal system which have enabled finance creditors to enjoy an advantage over employees. Well-informed (and industrially strong) employee groups might learn from the strategies commonly adopted by those other, powerful creditor groups.

AN ANATOMY OF THE NATIONAL TEXTILES CASE

If you trace through the corporate records held by ASIC on National Textiles, you will find that as early as 1 October 1999 the company was clearly in trouble. On this date, the company's major lender, the National Australia Bank, discharged fixed and floating charges over the company's assets because its loans were repaid. On the same date, new charges were registered in favour of two new lenders. One was Scottish Pacific Business Finance Pty Ltd, notorious as a lender of last resort, and the other was Oldtex Pty Ltd, a company associated with one of National Textiles directors and major shareholders, Philip Bart. Oldtex took a fixed charge over plant and equipment. This was a wise step for Oldtex, because under the *Corporations Act 2001* (Cwlth), ss. 433 and 556, floating charges only take priority in insolvency after payment of certain priority creditors (including employees).

These re-financing arrangements suggest that National Textiles' financial problems were known to its board, and its major creditor, as early as September 1999. No disclosure of this information was made to shareholders generally, nor to the market. National Textiles was at the time a listed company, obliged to comply with the Australian Stock Exchange listing rules, and the continuous disclosure requirements in the Corporations Act. Arguably, those rules would exempt disclosure of this type of information as being confidential, and generated only for the purposes of internal management of the company: (Koeck 1995; Hambleton 1997). In November 1999, the directors of the company, no doubt in the light of the added stresses and strains of managing a company through crisis, voted themselves a $103 000 increase in directors' emoluments (a tiny sum compared with the much publicised $7 million bonuses paid to two directors of One-Tel.) Shareholders learned of the deteriorating fortunes of the company at the annual general meeting on 30 November 1999. Many small businesses were still providing services to the company on credit, and of course the employees were still working, up until 20 January 2000 when an administrator was appointed to the company and the Australian Stock Exchange suspended trading in National Textiles shares.

FALLOUT FROM THE COLLAPSE

When the company collapsed, employees were owed about $11.1 million in unpaid wages, accrued leave entitlements, and redundancy payments. They were not the only losers. In many respects, some of the small unsecured creditors of the company, who were owed $14.49 million in total, suffered most. After the deed of arrangement, it was estimated that these people would receive less than 5 cents in the dollar. Of course, many truly independent businesses can factor the risk of bad debts into their prices. It is possible to buy insurance for bad trade debts. And if National Textiles was merely one of many customers of such a business, non-payment by that one debtor would not necessarily devastate the small business. But, according to newspaper reports, several of the small business creditors were ex-employees who had been 'contracted out'. For instance, *The Australian* ran a story on a truck driver who had moved from being an employee to a contractor working exclusively for National Textiles.[11] He was owed money for deliveries already done when the company folded. He was not entitled to share in the government-sponsored bail-out package, and people in his position are not entitled to claim under the General Employee Entitlements Redundancy Scheme. This is a matter of considerable concern when devising appropriate welfare-based responses to this problem. Any scheme which distinguishes between the employee and the dependent contractor in the costs it imposes on an employer will add to the pressure to outsource services, and will itself threaten worker security.

The big inside creditors don't appear to have lost anything. Scottish was repaid in full, and Oldtex was able to enforce its security over plant and equipment. According to the Report as to Affairs lodged by the managing controller of the company, the plant and equipment were valued in the books at $12 238 146, but had an estimated realisable value of $4 002 065.[12] These figures no doubt account for allegations made in Parliament that Oldtex acquired a factory worth more than $10 million in exchange for a $3.8 million loan.[13]

Of course, the other people who lost money were the minority shareholders who could no longer sell their shares when the Australian Stock Exchange de-listed the company. This is a salutary lesson for those who advocate employee share ownership as a solution to this problem. Any employee who also owned shares in National Textiles stood to lose twice out of the collapse.

Given the high level of media interest in this collapse, the Australian Securities and Investment Commission (ASIC) was quick to investigate and report on any allegations of corporate wrongdoing in this case. It found none.[14] This serves to illustrate that Australian corporate laws, as presently enacted, make it legitimate that corporate 'insiders' can arrange the affairs of the company so that they protect themselves from risk. Companies enjoy 'limited liability'. This means that the shareholders of a company can lose no more than the money they paid for the shares if a company becomes insolvent. If the company dies, owing more than it owns, the shareholders cannot be called upon to contribute to the company's losses.[15] This fundamental principle underpins investment in corporate enterprises. Very few people would invest in shares if they thought they could lose more than the price of the shares. It is a principle that is designed to encourage entrepreneurial investment and risk-taking. This principle, however, has spawned certain practices designed to ensure that corporate owners also protect their initial investment in the enterprise. They do this by contributing to the enterprise by way of loan, rather than capital, and they take security for the loan.

THE SALOMON DOCTRINE IN OPERATION

Students of elementary company law learn very early about the landmark case of *Salomon v A. Salomon and Co.* [1897] AC 22. This case was about a boot maker who decided to incorporate his boot making business early in the days of statutory limited liability. He made six members of his family nominal shareholders. They held only one share each, and they were obliged to hold the shares for their father on trust. Mr Salomon senior was the only true investor in the firm. He invested not by way of equity, but by lending to the company and taking debentures—in other words, he lent money to the company and took security. Later on, when the boot business was in decline (through no fault of his own), he sold his debentures to another person. When A. Salomon and Co. collapsed, the representative of all the unsecured creditors of the company argued—all the way to the House of Lords in England—that those debentures should not rank ahead of the company's ordinary creditors. They argued, essentially, that the controller of a company—the person who put the business enterprise into the market place—should not be able to rank ahead of the company's creditors in a winding up.

The House of Lords disagreed. The Law Lords said that it was the will of Parliament that a properly incorporated company should be a separate legal person—separate from those who incorporated it. The individual who gave life to the company is at liberty to contract with the corporation, on whatever terms he or she is able to secure from this company that he or she controls. If that means taking security over all of the assets of the enterprise, then—absent any proof of fraud—that security will be sound. That doctrine is at the heart of corporate practice in Australia. In fact, in many of the corporate collapses mentioned above, corporate assets have been secured by parties associated with the major shareholders and controllers of the company.

Take, for example, the Steel Tank and Pipe group of companies, some of which fell into the hands of receivers in November 2000. The companies employing the staff were the ones to become insolvent. A search of the company register of several of the myriad companies in this complex group showed that many of the companies had paid-up capital (that is, shareholder funds) of $2. The largest capital contributions were $1000. All of the shares were owned by persons with the name 'Weeks'. At the same time, a person by the name Margaret Violet Weeks had the benefit of a fixed and floating charge over all the assets of 18 companies in the group, to the tune of $20 million. These charges were registered on 27 October 2000. Several of the companies went into receivership on 8 November 2000. Mrs Weeks, who was the mother of the two brothers controlling the group, had been a director of the company, but she retired or resigned on 21 December 1999. This was very fortunate for her. The insolvent trading provisions in Part 5.7B of the *Corporations Act 2001* (Cwlth) make it very risky these days for a major secured creditor to take a seat on the company's board. Even non-executive directors can be held liable for a company's losses if they allow the company to trade while insolvent.

This case is another illustration of the fact that corporate law allows the owners of the company to protect themselves from risk. The argument that the owners of corporate enterprises bear the most risk because they put up the capital becomes nonsensical if the share capital of a company stands at $2. Or even $1000. Well-advised owners can protect their investment in a company very effectively by contributing very little as share capital, and the bulk by way of secured loans.

The owner-lender to corporation can acquire a property interest in the assets of the corporation because, although a loan arrangement is a contract creating personal obligations to repay, it can also create property rights. Our legal system has been very creative in devising and recognising ways in which finance creditors can convert contractual rights into property rights. A simple clause in a contract, supported by registration of information on a public register, will create a property right over a company's assets for a creditor who lends money to the firm.[16] This is because courts exercising equitable jurisdiction have been willing, for over a century, to order specific performance of promises to convey property. To take a very simple example: A lends B $100 and, in exchange, B makes two promises: (1) B will repay the $100 with interest, and (2) if B fails to repay on time, B will convey B's television set to A. A now has a security interest in B's television set, because a court will specifically enforce the promise to convey the television set if B defaults on the loan. This is better than a mere right to damages, because A will be able to claim the television set ahead of anyone else to whom B owes money. This is what happens when a company fails to repay a finance creditor. The creditor's rights under the loan contract enable the creditor to claim ownership of the assets used as security. Those assets now belong to the creditor, and they are not available to be sold to meet the liabilities to other creditors, including employees.

CONTRAST THE POSITION OF EMPLOYEES

Employees also invest in corporations. They invest—or perhaps a more apt word is 'exhaust'—their human capital in the firm. They commit time and energy, talents and skills. Many organise their lives around the demands of the enterprise.

But the legal conception of the employee's relationship with the enterprise is not as an investor, but as an external service provider. As far as the law is concerned, the employee is an outside creditor who contracts to provide services to the company in exchange for wages and other benefits. Contracts for services have traditionally not been specifically enforceable. That is, if contracting parties breach the contract, a court will award damages, but will not order that the contract be performed. When the contract is terminated, the employee has no residual property interest in the firm, only an entitlement to be paid any outstanding wages or entitlements. That entitlement does not automatically attach to any specific property owned by the employer. Finance creditors who have contracted for property rights in the event of default will lay first claim to the employer's assets.

In recent decades the Australian community has recognised the investment that long-serving employees make in enterprises through the evolution of termination, change and redundancy provisions in awards and agreements. In the *Termination Change and Redundancy Case* (1984) 8 IR 34, heard by a full bench of the Australian Conciliation and Arbitration Commission in August 1984, it was held that employees who lost their jobs due to redundancy should be entitled to severance pay, in addition to payment of notice on termination. The Commission made it clear (at p. 73) that the reasons for awarding severance pay were not simply to 'tide over' an employee for a period of unemployment: 'We prefer the view that payment of severance pay is justifiable as compensation for non-transferable credits and the inconvenience and hardship imposed on employees'. Those non-transferable credits recognise the 'opportunities foregone in the continuous service of their employer'. This is some small recognition of the investment of human capital that a long-term employee makes in a firm. That test case awarded:

- 4 weeks for between one and two years of service,
- 6 weeks for between 2 and 3 years,
- 7 weeks for 3–4 years, and
- 8 weeks for more than 4 years.

(These redundancy benefits were granted by the AIRC to the One-Tel employees in their urgent interim award made on 5 June 2001: *CPSU and One-Tel Ltd*, Print C2001/3253.)

Since the 1984 test case, enterprise agreements in some industries have provided more generous benefits. Recognising these entitlements is only part of the problem. The main difficulty is ensuring that those entitlements are actually paid. These entitlements, like wages and accrued annual and long service leave, constitute a *personal*, contractual right that the employee has against the company. If a company becomes insolvent, those personal rights will rank behind any property rights that other creditors have in the assets owned by the company. Any secured creditor will have property rights in company assets, which rank ahead of unsecured creditors like employees.

Presently, employees enjoy the benefit of two measures which purport to deal with the disadvantage that flows from being a service provider, and therefore an unsecured creditor. The first is the statutory priority for employee entitlements in sections 433 and 556 and of the *Corporations Act* 2001, which rank employees' claims ahead of floating charges, as well as ahead of other unsecured creditors. And the other is the welfare safety net, presently provided by GEERS. Some may assert that there is no need to bother with the trouble of securing entitlements while these measures are available. Let us examine that assertion.

STATUTORY PRIORITY

Presently, the *Corporations Act* section 556 lists certain priority creditors in a winding-up. After the liquidators' various costs, comes paragraph (e) 'Wages and superannuation contributions payable by the company in respect of services rendered to the company by employees before the relevant date'. Next in line is (f) injury compensation payments, then (g) all amounts due, because of an industrial instrument, in respects of leave of absence. 'Leave of absence' is defined in section 9 as 'long service leave, extended leave, recreation leave, annual leave, sick leave or any other form of leave of absence from employment'. Finally comes (h) retrenchment payments payable to employees of the company. 'Retrenchment payment' is defined in section 556(2) as an amount payable 'by virtue of an industrial instrument'. 'Industrial instrument' is defined in section 9 of the Act to mean a contract of employment, or a 'law, award, determination or agreement relating to terms or conditions of employment'. The section excludes any employees who are or have recently been directors of the company and their family members from full enjoyment of this priority. (Such people can claim no more than $2 000 in wages and superannuation contributions, $1 500 in leave of absence payments, and nothing in respect of retrenchment.)

Notably, section 560 allows any person who advances money to a company for the purpose of meeting claims which would enjoy priority under section 556, to stand in the shoes of those claimants. This is a statutory right of subrogation. It is the right that the federal government presently claims when it has paid any entitlements under the EESS or GEERS. It claims an entitlement to recoup any payments from the liquidators, ahead of payment to other unsecured creditors. Some of those small business creditors (particularly the out-sourced contractors) have understandably complained about this right of subrogation.

This list of priorities ranks unsecured creditors after secured creditors, but before floating charge holders (see section 561). Before the November 2001 federal election, in the midst of the Ansett debacle, the Prime Minister, the Hon. John Howard, announced in the media that the government would consider re-ranking employee entitlements, ahead of secured creditors. This proposal would not be as simple as it appears on its face. What kind of security arrangements would be included? Would sale and lease-back arrangements also be caught, so that the title-holders of assets leased to a business would be forced to surrender them up to meet payment of employee entitlements? This is a proposal that can only be assessed properly when detailed legislation is available. At this stage, employee claims rank behind all but floating charge security.[17] Of course, the real trouble with a priorities system is that first bite of nothing is still nothing. While employee entitlements continue to rank after secured creditors, and after those highly qualified and hence highly paid company liquidators, there will often be less than enough left to pay employees.

THE EESS AND GEERS

The Australian Law Reform Commission conducted a General Insolvency Inquiry, Report No. 45, which reported in September 1988 on these priority provisions. The Report noted criticisms of the priority system, and recommended that a 'wage-earner protection fund' would better address the problem (see paragraph 727). To some extent, that is what we now have in the GEERS (and its predecessor the EESS). It is also what has been created specially for Ansett employees by the airline ticket levy scheme.[18] While these taxpayer-funded (or in the case of Ansett, consumer-funded) schemes are certainly better than nothing, they have their critics.

One source of criticism, levied particularly at the EESS, was that it was not generous enough. It didn't guarantee payment of all entitlements. The federal proposal was to cap payments at $20 000 per employee, but this was on the basis of joint funding by state and federal governments. For a long time, all state governments declined to participate (South Australia alone electing to join in at a late stage), so the maximum payment to any individual employee was $10 000. To receive this maximum, an employee would have to be on a salary of at least $40 000 per annum, and have lost at least 4 weeks' wages, 4 weeks' annual leave from the past 12 months, 5 weeks' pay in lieu of notice (this is the amount due under s. 170CM of the *Workplace Relations Act* 1996 for an employee who is over 45 and has a minimum of 5 years service), 4 weeks' redundancy pay, and 12 weeks' long service leave. The GEERS scheme, effective from 12 September 2001, is considerably more generous.[19] It promises to pay all unpaid wages, all accrued annual leave, all accrued long service leave, all accrued pay in lieu of notice and up to 8 weeks redundancy entitlement. Benefits are capped, based on a maximum salary of $75 200 per year. Even though it is more generous, it still doesn't guarantee payment of full retrenchment benefits to long serving employees who have often foregone present pay rises for the promise of greater security through more generous retrenchment payments. Eight weeks' redundancy is still a small entitlement for a person with decades of service.

At another level, these welfare schemes have been criticised as constituting a taxpayer-funded subsidy to business.[20] Should taxpayers be obliged to underwrite corporate losses? Taxpayers are entitled to resent this call on the social security purse, when they see frequent stories about large companies which pay very little tax, and they see stories about share price hikes, and massive pay-outs to executives.

As was noted at the outset, there have been proposals for industry-funded rather than taxpayer-funded schemes. One of the proposals which has been considered by both major political parties is an insurance scheme, whereby large employers would pay premiums to insure the risk of lost entitlements. The New South Wales Department of Industrial Relations commissioned Benfield Greig (an independent reinsurance broker and risk adviser) to undertake a feasibility study into the provision of a National Insurance Scheme to protect employee entitlements (report dated 29 July 1999). This report suggested that the most efficient scheme to run would be a flat-rated compulsory scheme, which was tied into Workers Compensation cover. The Federal government has investigated this and other insurance-based proposals and has concluded that they are simply not viable (Abbott 2001). The reasons (which are not canvassed in any detail in this paper) include the reluctance of the private sector insurance industry to provide cover for a risk which is not well known, the additional costs to employers, especially those stable businesses who would be subsidising their weaker competitors, and the allegedly high administrative costs such a scheme would involve.[21] The year 2001 was also the year of the HIH insurance collapse, so perhaps it is not surprising that investigation of insurance solutions to this problem has stalled.

Another suggestion, which has borne some fruit in the form of the ManuSafe trust scheme described briefly above, is the institution of industry trust funds. These are particularly supported by unions who are familiar with the success of long service leave funds. They involve the imposition of obligations on employers to contribute an amount to meet entitlements as they accrue. The Minister's paper (Abbott 2001) pours cold water on these proposals, though not without conceding that the EESS was a safety net only and did 'not preclude the adoption of additional measures, by particular employers and employees', on an agreed basis. As a national compulsory scheme, however, the Minister criticised the trust fund proposal because it would withdraw working capital from industry in order to set aside money for payments which may never in fact fall due. It is true that often employees take their holidays and their long service leave. Often they resign or are dismissed without receiving any redundancy pay. Any scheme which required employers to set aside the full dollar amount of any contingent debt to employees may well over-compensate. Another pragmatic concern is that an employer in strife is likely to cease paying its contributions to such a trust anyway, just as it ceases paying all other claims.

SPECIFIC SECURITY ARRANGEMENTS

This leads us, finally, to our destination: a consideration of whether it may be possible to devise strategies for employees to obtain the same kind of security obtained by finance creditors (like Scottish Pacific and Oldtex in the National Textiles case). Those creditors do not withdraw assets from the corporate enterprise while it is a going concern, however, they manage to assert a full proprietary interest on insolvency.

It is entirely feasible that a fund may be set up that did not involve the withdrawal of working capital from the enterprise. In other areas of commerce, the concept of a security trust is well known. This is how it works. The corporate employer would agree to grant a fixed charge over certain assets (such as Oldtex took over National Textiles' plant and equipment) to secure payment of all employee entitlements as they fell due. This security would be held on trust for the employees. The trust is a suitable vehicle for holding the security, because it overcomes any obstacles created by the doctrine of privity of contract. In *Ryan v. Textile Clothing and Footwear Union of Australia* (1996) 66 IR 258, Hayne J held that an unregistered collective agreement was not legally binding, and one of the reasons for this was that many of the employees purportedly covered by the agreement had never been parties to the agreement. By using a trust, it would not be necessary for any individual employee to consent to the arrangement, or even know about it. The trust deed could be so drawn as to define the class of beneficiaries as all employees of the company who, at the date of the default event, were owed any accrued entitlement. This means that any new employees joining the company would automatically be included in the arrangement. If the company used many dependent contractors (i.e. former employees moved onto contract arrangements, but who still worked solely for the employer), the class of beneficiaries might be expanded to include these workers as well.

The creation of the security trust would not involve any withdrawal of working capital from the enterprise while it was a going concern. The security held by the trustee would be nothing more than the benefit of a contract, so drafted to be effective to grant the trustee a right to assert a property interest in the assets subject to the security, should the employer default on the terms of the agreement. (Of course, this security would need to be registered as a company charge.) The employer's failure to pay any entitlement when it fell due could be defined as a default event, entitling the trustee to call on the security. So there need be no actual withdrawal of funds from the corporate enterprise. There would be some administrative costs, but then corporate borrowers have coped with the bank fees and charges associated with secured overdrafts in the past, so why not the fees associated with this type of account? This is by no means a novel arrangement. External professional advisers to companies (such as architects, accountants, auditors and lawyers) regularly take security for their fees in this way. Why should the employees who work within the company be barred from bargaining for the same kind of protection?

One of the arguments raised against extending these security arrangements to employees is that banks wouldn't tolerate it. Competition from secured employee claims would put the banks' privileged position in corporate insolvency at risk, so they would refuse to lend, or raise the price of finance, to a company with this type of scheme in place. Given that banks are primarily in the business of lending and are expert in credit risk management, it is difficult to imagine that banks would not acclimatise to these schemes if they became prevalent in the market place. The banks may even begin to fulfil a valuable service by monitoring corporate health not only for the benefit of their own shareholders and depositors, but for the benefit of the company's employees and other creditors. And we should also remember that in the National Textiles case, the National Australia Bank had already exited the company. The secured creditor competing with employees in this case was a company associated with a major shareholder.

On its face, the Prime Minister's proposal (discussed above) that employees entitlements should rank ahead of secured creditors, would defeat any need for such security devices. That may be so, however the following points should be noted:

1. A legislated scheme will be hedged around with definitions of what types of employee entitlements will enjoy the priority. Bargained for security arrangements leave these definitions in the hands of the parties themselves, unaffected by political winds.

2. A legislated scheme will also need to define what types of security will be postponed. There are many creative forms of security which don't look like security at all from a legal point of view; the sale and lease back arrangement being one of them. A negotiated solution would enable the parties to stipulate for themselves what assets would be available for employees in the case of insolvency.
3. A legislated solution continues to exclude employees from insider knowledge of the company. Big financial creditors, by virtue of their security arrangements, often enjoy rights of inspecting financial records, and knowing what the financial health of an organisation is, often before the market generally. Again, the National Textiles case study is illuminating. Employees, through their representatives, might also enjoy better access to information about the financial health of the enterprises they work for if they negotiate security arrangements. This inside knowledge may well lead to improved corporate governance and greater involvement of labour interests in the management and control of corporate enterprise. This point is worth particular elaboration.

Improved corporate governance

The very existence of trustees who hold securities on behalf of employee beneficiaries would introduce a party with an interest in monitoring the health of the corporate employer in the interest of stakeholders other than shareholders. Such supervision may help to avoid some of the worst cases of corporate manipulation which use corporate group structures. The typical scenario involves a group of companies, all owned by the same shareholders and all managed by the same directors. One company in the group employs the workers, while others in the group own all valuable assets. Well-informed financiers often insist on dealing only with the asset-rich member of the group, but employees are often quite unaware that there are several different companies in the group. The undercapitalised employer company is the first to fail in a downturn, enabling the group to shed labour, and avoid payment of redundancy benefits.

Legislation which would have the effect of lifting the veil between companies in a corporate group was proposed by ALP members of federal Parliament after the Waterfront dispute.[22] The idea behind this legislation was that other companies in a group who had contributed to the management of a failed company might be held liable to meet obligations to a failed company's employees, in circumstances where a judge held it would be just to do so. The Minister's paper (Abbott 2001) states that this proposal was considered by the Companies and Securities Advisory Committee, which did not support its introduction. This is not surprising. The proposal challenges the entrenched doctrine that each incorporated association is a separate legal person, despite affiliations with other corporations. Courts have only rarely been prepared to lift the veil on corporations, and hold one company (or its members) liable in any way for the debts of another.[23] And yet, in some of the more notorious cases, there have been allegations that the controllers of a group have deliberately exploited this doctrine so as to preserve property for themselves, while ensuring that employees go away empty-handed. Measures which prohibit the deliberate under-capitalisation of an entity in a group which employs staff would seem to be an obvious solution in those cases where manipulation of the corporate form can be proven. In the absence of legislative provisions, the establishment of 'employee entitlements security trusts' under the control of trustees who are entitled to inspect company books to fulfil their duty to protect the interests of beneficiaries, may at least provide an early warning system where such manipulation is going on behind the scenes.

MORE RADICAL SOLUTIONS

Those who consider 'lifting the veil' on groups too radical a solution to this problem, will also reject calls for greater participation by employees in corporate governance. And yet, this is by no means a new idea. In Germany, for instance—surely a successful industrial economy—worker representation at board level has been mandated for large enterprises for many decades (Vorbrugg 1977). In Australia, McCallum (1997) has advocated new forms of worker participation, via Work Councils, properly tailored to meet Australian conditions. Bray *et al.* (2001) also recommend urgent attention to improving worker participation in Australian industry, to address the 'representation gap'. Better avenues for employee participation, or at least consultation, in corporate decision-making may at least address the injustice apparent in those cases where well-informed insiders have been able to parachute out of a problem company, leaving employees and unsecured creditors to bear the full brunt of corporate losses. If companies are to be structured so as to place considerable risk on the shoulders of employees, then surely it is only fair to consider appropriate mechanisms for them to be consulted in decisions relating to the management and performance of the enterprise.

THE CHALLENGE

The challenge now is for employee representatives and their lawyers to dig out the security trust precedents from their legal document databases, and consider how they might be adapted to provide some better protection for employee entitlements. Then the task will be to negotiate with employers, in the course of bargaining for collective agreements, for the establishment of these trusts. It will take considerable industrial muscle. Many employers can be expected to resist inclusion of such measures in industrial agreements, just as they resisted the introduction of 'termination, change and redundancy' clauses in awards when they were first proposed.

Nevertheless, it is a task worth undertaking. As was demonstrated by the One-Tel story (which occupied national broadcast and print media from May to July 2001), today's workforce is particularly vulnerable in corporate collapse. Those employees were largely very modestly paid workers, with no retrenchment entitlements until the Communications, Electric, Energy, Information, Postal, Plumbing and Allied Services Union of Australia came to their aid and sought an urgent award. The One-Tel employees were all 'new tech', information industry workers. This was not just another case of the dislocation felt when an obsolete industry begins to crumble. It was an all too typical scenario of a business run inefficiently by executives who were none too shy of taking generous rewards for themselves. In the One-Tel and National Textiles cases, the community showed strong support for providing redundancy benefits for workers, and ensuring that they were paid. The GEERS was a straightforward solution to providing a minimum safety net. But questions remain. Why must employees settle for the minimum? Why should they not also enjoy the full benefits of their investment in an enterprise, especially when they have traded off current pay and benefits for long term security in the form of larger retrenchment benefits? And why should the general taxpayer fund any entitlements, when corporate profits have been syphoned off into luxury lifestyles for the former directors of failed enterprises? Why not move toward developing strategies whereby corporate enterprises internalise and make provision for their own costs of production? The specific security trust proposal outlined in this paper is one strategy for improving employees' chances of being paid their full entitlements by the enterprise which ought to pay those entitlements. It is hardly radical. It employs legal tools which have been available to other creditors for over a century. It does not extract working capital from industry. And it may offer long term benefits of improved corporate governance in Australian enterprise, because more of the stakeholders in the enterprise will have an interest in and entitlement to supervise and perhaps even participate in management.

One fearful objection is often raised. What about jobs? Isn't it better to just turn a blind eye to the corporate rorts, and keep people working in the dark for as long as possible? Who cares if the taxpayer picks up the bill in the end? In this writer's view, some commentators over-emphasise the importance of keeping jobs alive at any cost. We need a new vision of the Australian corporate landscape. Australian corporate enterprise should be more efficient and productive (which means bearing its own costs) but also more equitable. That will inevitably mean greater partnership between the shareholders, the executives and the non-executive employees, in sharing the risks and returns of the enterprise. The security trust proposal does not shield employees from all risk. It treats them as dignified and autonomous human beings who are entitled to knowledge about those risks, opportunity to bargain over how they will price those risks, and access to the full range of legal tools to manage those risks.

NOTES

1. Toni O'Loughlin 'Play it safe and take that holiday, says Abbott'. *Sydney Morning Herald* 23 January 2001, p. 3.
2. These figures are taken from a report by Jeff Corbett, published in the *Newcastle Herald* on 15 November 2000, p. 8, and available from the Dow Jones Interactive Web-site at http://ptg.djnr.com/ccroot/asp/publib/story.as, last visited 3 February 2001.
3. The Benfield Greig Report commissioned by the NSW Department of Industrial Relations cites 'a general paucity of data to support any detailed analysis' of this problem. See *National Insurance Scheme to Protect Employee Entitlements*, *Preliminary Feasibility Study*, 29 July 1999.
4. For example, Oakdale Collieries, Cobar Mines, Grafton Meatworks, Parrish Meatworks, to mention a few cases which have made headlines in recent years.
5. The Federal and NSW governments each contributed $2 million. See Louise Dodson and Chelsea Martin 'Howard Bails out Workers', *Australian Financial Review*, 9 February 2000, pp. 1,4. The bulk of the federal government's share of this contribution was paid out of a fund set aside for the Regional Assistance Program, designated to foster regional employment

growth. See Chelsey Martin 'New Heat over Textiles Bailout', *Australian Financial Review*, 19 June 2000, p. 3.

6. These figures come from the Employee Entitlements Support Scheme One Year Activity Report, January 2001, available at http://www.dewrsb.gov.au/default.asp, last visited 7 June 2001.
7. At the time of writing, the Corporations Act 2001 (Cwlth) had just been given Royal Assent. To avoid confusion, this paper refers to the legislation as the Corporations legislation, rather than the 'Law' or the 'Act'.
8. Both major political parties have investigated the feasibility of insurance-based schemes. At the time of writing, the NSW Department of Industrial Relations continued to support a proposal to introduce compulsory insurance along the lines of a workers' compensation scheme. See an on-line press release issued by the Department at http://www.dir.nsw.gov.au/about/minister/press/300799.html/, last visited 13 June 2001. The federal government has investigated this proposal and dismissed it as impractical. See Abbott (2001).
9. The most convenient source of information on the ManuSafe proposal is available on-line at http://www.manusafe.com.au
10. See *Workers Online*, Issue 109, 31 August 2001, at http://workers.labor.net.au/109/news43_manusafe.html, last visited 10 January 2002. The unions involved in negotiating with the Tesna syndicate during the aborted attempt to salvage Ansett Airlines had made some progress in a deal to secure employee entitlements by way of a charge over the airport terminals before the deal collapsed.
11. *The Australian*, 23 February 2000.
12. Form 507 Report as to Affairs lodged with ASIC on 29 February 2000 by VC Barilla, Joint Receiver and Manager.
13. Simon Crean, Hansard, House of Representatives, 15 February 2000, p. 13428.
14. See Martin A, 'Watchdog puts PM's brother in the clear' *Australian Financial Review*, 9 August 2000, p. 4.
15. The exception to this rule is when shareholders have been issued shares on an unpaid or partly-paid basis, in which case the shareholder will be required to pay the unpaid component of the purchase price to the company on liquidation.
16. For an illuminating discussion on the development of the equitable charge, see Nkala (1993).
17. This article takes into account legislation tabled up to 31 December 2001.
18. See the *Air Passenger Ticket Levy (Collection) Act* 2001, No. 132 of 2001, and the *Air Passenger Ticket Levy (Imposition) Act* 2001, No. 133 of 2001, both passed and assented urgently on 27 September 2001 in the wake of the Ansett collapse.
19. See Abbott T, Media Release dated 20 September 2001 'Even better arrangements to protect employee entitlements', http://www.dewrsb.gov.au/ministers, last visited 3 October 2001.
20. See, for instance, criticism levelled by former Liberal leader, John Hewson, in 'Howard's ties lead to bind', *Australian Financial Review*, 11 February 2000, p. 15; also, Kohler A, 'Family Ties Undo Fair Policy', *Australian Financial Review*, 15 February 2000, p. 20; Editorial 'Keep politics out of payouts' *Australian Financial Review*, 9 February 2000, p. 16.
21. Not all commentators are so pessimistic about the costs of an insurance solution. See for instance the opinion page commentary by Ron Callus, 'Employees' entitlements up in the Air', in the *Canberra Times*, 17 September 2001, p. 11, which cites an estimated cost of $20 per year per employee to fund such a scheme.
22. Arch Bevis, ALP Federal member for Brisbane, and Senator Jacinta Collins tabled identical private member's bills, both named the *Employment Security Bill* 1999, following the waterfront dispute.
23. Cases include Walker v. Wimborne (1976) 137 CLR 1; Industrial Equity Ltd v. Blackburn (1977) 137 CLR 567 and Pioneer Concrete Services v. Yelnah Pty Ltd (1987) 5 ACLC 467.

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