ASIC
Australian Securities & Investments Commission

Senate Inquiry into the Conduct of Insolvency Practitioners and ASIC's Involvement

Further submission by the Australian Securities and Investments Commission

June 2010

Contents

A Executive summary

1 The Australian Securities and Investments Commission (ASIC) makes this further submission to assist the Senate Economics Committee with its inquiry into the role of liquidators and administrators, their fees and their practices, and the involvement and activities of ASIC before and after the collapse of a business (the Inquiry). This submission supplements our first submission dated 7 March 2010, our letter of 12 April 2010 and our appearance before the Inquiry on 12 March 2010.

2 During the public hearing in Canberra on 12 March 2010, the Inquiry asked that we provide additional comments about a number of matters, including the role of receivers and managers, as if they had been included in the original terms of reference. This material has been included in Appendix 1.

3 The main part of this submission, Section B, provides our comments on a range of issues raised during the public hearings. We have made comments on those various issues, grouped under three headings:

(a) improving standards;

(b) improving oversight; and

(c) oversight of directors in small-to-medium enterprises (SMEs).

4 Table 1 summarises the specific topics that we have provided further comment on, grouped under the three key categories as noted above.

Table 1: Outline of ASIC areas of comment on issues raised through public hearings

Issue	Areas of ASIC comment
Improving standards	• Licensing regime compared with the existing registration regime • Professional indemnity cover
Improving oversight	• Increasing ASIC's surveillance • Penalties • Role of the industry ombudsman
Oversight of directors in SMEs	• Phoenix company activity

5 We have provided additional information about the estimated additional resources that may be required as a result of the possible adoption of the suggestions discussed during the course of the public hearings.

6 Table 2 provides a summary of the estimated additional resources, with references to the relevant paragraphs in Section B, where the suggestions are discussed in more detail.

Table 2: Outline of additional resources required should the suggestions of the Inquiry be adopted

Suggestion	Additional full-time equivalent staff members (FTEs)		Paragraph reference
	Start-up FTEs	Ongoing FTEs	
Ability to place conditions on registration of liquidators	4	1.5	29
Introduction of licence/ registration renewal period	2	7.06	33
Introduction of interview panel as part of liquidator registration process	1	0.14	36
Increasing ASIC surveillance resources	*	65	65
TOTAL	**7**	**73.7**	

* This assumes that there are no start-up FTEs associated with the change in surveillance approach, due to the internal nature of the decision and the existing surveillance function being performed. The estimate for increasing ASIC's surveillance resources assumes annual surveillance reviews. If biennial surveillance reviews occurrred, 31 ongoing FTEs would be required for those reviews, with the total FTEs required to introduce all the changes reducing to 39.7.

ASIC's submission

7 As noted, this further submission sets out our comments about issues raised during the public hearings before the Inquiry. For example, we provide details of the Government's previous consideration of a licensing regime for insolvency practitioners in 2007 and the improvements ultimately adopted by the Government at that time through the Corporations Amendment (Insolvency) Bill 2007.

Appendixes

8 We have provided further detail relating to sections of this submission in appendixes, as follows:

(a) Appendixes 1 and 2 provide information about the addition of receivers and managers to the original terms of reference;

(b) Appendix 3 provides, for the information of the Inquiry, a copy of our recent Media Release (MR 10-90) *113 Company officers prosecuted in three months*, which advises of the summary prosecutions between January and March 2010; and

(c) Appendix 4 provides confidential information, and sets out our answers to the questions on notice put to ASIC during our appearance at the hearing of 12 March 2010, our comments on previous ASIC submissions on phoenix company activities, and confidential detailed costings associated with our estimated additional resources.

B ASIC's response to issues raised during the public hearings

Key points

The public hearings have raised a number of suggestions as to improved regulation for the insolvency profession. To assist the Inquiry, we have provided further comment regarding:

- improving standards for insolvency practitioners;
- improving oversight for insolvency practitioners; and
- oversight of directors in SMEs.

9 Table 3 provides an overview of our responses to the issues raised during the public hearings.

Table 3: Overview of our responses to issues raised during the public hearings

Issue	ASIC response	Section B reference
Improving standards		
Licensing regime compared with the existing registration regime	Licensing regime compared with a registration regime	See paragraphs 10–33
	ASIC's existing liquidator registration process—Consideration of an interview panel as part of the existing registration process	See paragraphs 34–36
	Broadening the base of practitioners	See paragraphs 37–38
Professional indemnity cover	To assist the Inquiry, we have provided further commentary on issues surrounding professional indemnity cover and its availability, including the role of 'run-off' cover	See paragraphs 39–50
Improving oversight		
Increasing ASIC's surveillance	ASIC's forward program—As previously outlined in ASIC's original submission, two key projects that are currently in progress are those on remuneration and independence	See paragraphs 53–58
	ASIC's surveillance approach—We have provided a comparison of the surveillance approach adopted by the Insolvency and Trustee Service of Australia (ITSA) and that used by ASIC	See paragraphs 59–65

Issue	ASIC response	Section B reference
Penalties	We have made further comments on penalties for liquidator misconduct, including the use of the Companies Auditors and Liquidators Disciplinary Board (CALDB)	See paragraphs 66–70
Role of an industry ombudsman	It is unclear what role an industry ombudsman would have if a licensing system were adopted. We have provided an outline of the objectives and operation of the Financial Ombudsman Service (FOS) to illustrate an alternative dispute resolution mechanism that already exists for Australian financial services (AFS) licensees	See paragraphs 71–79
Oversight of directors in SMEs		
Phoenix company activity	We have provided an outline of our recent response to Treasury on its proposal paper *Action against fraudulent phoenix activity*	See paragraph 80 and confidential Appendix 4

Improving standards

Licensing regime compared with a registration regime

***Key issue**: Is the current registration regime for insolvency practitioners adequate or should a licensing regime be introduced?*

10 The Inquiry has heard submissions that, in a number of situations, the existing registration regime for insolvency practitioners is not effective in dealing with concerns about:

(a) the varying levels of experience of insolvency practitioners and the assessment of fit and proper person requirements at the time they become registered; and

(b) the means by which to suspend or cancel an insolvency practitioner's registration in situations where there is evidence of misconduct by the insolvency practitioner.

11 It has been suggested that a licensing regime may be more appropriate than a registration regime because it would allow for greater flexibility on the conditions of an insolvency practitioner's practice, as well as providing a clear method of redress in circumstances of practitioner misconduct.

12 A comparison between ASIC's current insolvency practitioner registration regime and the current AFS licensing regime highlights the key differences between a registration and a licensing regime (see Table 4).

Table 4: Comparison between registration and licensing regimes under the Corporations Act

Registration obligations	AFS licence obligations
Obligations under s1282 Where ASIC must grant application for registration as a liquidator: • the applicant must hold relevant qualifications • the applicant must have appropriate experience • ASIC must be satisfied the applicant is capable of performing duties of a liquidator (i.e. is fit and proper) ASIC must not register a disqualified person Registration remains in force until cancelled, or suspended by CALDB or ASIC, or the person dies	**Obligations under s912A** • Services must be provided efficiently, honestly and fairly • There must be adequate arrangements to manage conflicts of interest • Licence conditions must be complied with • Financial services laws must be complied with • Representatives must comply with financial services laws • Adequate resources (financial, technological and human resources) must be maintained • Competence to provide services must be maintained (requirements around qualifications and training are further set out in Regulatory Guide 105 *Licensing: Organisational competence* (RG 105)) • Representatives must be adequately trained and competent • There must be internal dispute resolution (IDR) processes for complaints by retail clients (to ASIC standard/requirements) • The licensee must be a member of an external dispute resolution (EDR) scheme for complaints by retail clients (to ASIC standard/requirements) • There must be an adequate risk management system • Any other obligations as prescribed must be complied with • Requirements as to good fame and character must be met
Obligations under s1284 Insurance to be maintained by liquidators: adequate and appropriate professional indemnity and fidelity cover must be maintained	**Obligations under s912B** Compensation arrangements: licensees must have compensation arrangements for retail clients (predominantly professional indemnity insurance) for loss or damage suffered due to breaches of obligations
Obligations under s1287 Liquidator events that require notification: • ceasing to practise as a liquidator • change of liquidator name • change of liquidator address • suspension of liquidator • disqualification from managing corporations	**Obligations under s912C** Direction to provide a statement: • ASIC may direct that a written statement be provided to ASIC • ASIC may direct the licensee to obtain an audit report

Registration obligations	AFS licence obligations
Obligations under s1288	**Obligations under s912D**
Annual statement by registered liquidator covering: • liquidator details (e.g. name, address) • current status of liquidator's practice • capacity in which liquidator is practising • practice details • professional membership • continuing professional education • residency • disciplinary action or convictions • professional indemnity insurance details	Obligation to notify ASIC of certain matters: • A licensee must notify ASIC of breaches/likely breaches of any obligation under s912A or 912B, a financial services law, or applicable Commonwealth legislation • Whether a breach/likely breach is significant is based on factors such as the number or frequency of breaches, the impact of the breach on the licensee's ability to provide financial services, whether the breach indicates that the licensee's compliance arrangements are inadequate, and the potential/actual loss to clients of the licensee or the licensee itself

13 The general obligations of AFS licensees under s912A provide a basis to address concerns about variable levels of experience of insolvency practitioners through the ongoing requirement to ensure that the licensee and their representatives are competent. These requirements also provide a mechanism through which to address practitioner misconduct by allowing the suspension or cancellation of a licence.

14 In a situation where we may seek to cancel, suspend or vary a licence, we need to afford the licensee the right to appear before a hearing on the proposed action on their licence, and the right to appeal any decision to the appropriate authority (i.e. the Administrative Appeals Tribunal (AAT)).

15 Additionally, the requirements of s912A and 912B for AFS licensees ensure that the licensee not only has appropriate IDR processes in place, but that they are also a member of an EDR scheme. These elements of a licensing regime may address the concerns of the Inquiry as to the 'protection' of creditors and the possible resolution of their complaints.

16 To assist the Inquiry further with its consideration of a licensing regime, we have provided further information on:

(a) the previous consideration of a licensing regime (as part of the Corporations Amendment (Insolvency) Bill 2007 (2007 Amendments));

(b) s1289A of the Corporations Act, which enables conditions to be placed on the registration of an auditor. This is a regulatory model that combines elements of both a registration regime and a licensing regime; and

(c) the estimated additional resources required if a licensing regime is adopted with a 'renewal' period (i.e. where the licence is only issued for a specified period of time).

17 As part of our outline of s1289A, we have also provided an estimate of the additional resources required to implement a similar regime for the registration of insolvency practitioners: see paragraph 29.

Previous consideration of a licensing regime

18 Following are some key comments made as part of the regulatory impact statement to the 2007 Amendments. These comments provide some background to the current registration regime for insolvency practitioners, compared with a possible introduction of a licensing regime.

19 As part of the considerations to the 2007 Amendments, the introduction of a licensing regime for insolvency practitioners was considered but not adopted by the Government. This option included:

(a) the requirement for the regular renewal of licences to facilitate regular monitoring of matters (such as compliance with continuous education standards and maintenance of practice capabilities);

(b) provision for the cancellation of licences at an administrative level (without seeking the approval of CALDB);

(c) the provision of conditional issuing of licences;

(d) more active monitoring of insolvency practitioners by ASIC; and

(e) the provision of ongoing obligations to perform adequately and properly the duties of a registered liquidator, to remain a fit and proper person, to comply with conditions of registration as prescribed by ASIC or the regulations, to maintain professional skills, to maintain adequate practice capabilities, to notify ASIC if practitioners become disqualified from registration, to lodge annual statements and to maintain arrangements for compensation for loss.

20 Rather than a licensing regime, the Government retained the existing registration regime, with the inclusion of some additional targeted amendments.[1] These targeted amendments to the registration regime were designed to:

(a) improve the quality and reliability of information available to creditors in considering the appointment of insolvency practitioners;

(b) update the experience criteria for initial registration of practitioners;

(c) strengthen the ongoing requirements for registration;

(d) prohibit the offering of inducements to directors and other persons to obtain appointments; and

(e) introduce more flexibility for creditors to replace administrators.

[1] Refer to the Corporations Amendment (Insolvency) Bill 2007: http://www.comlaw.gov.au/ComLaw/legislation/bills1.nsf/bills/bytitle/6DCBDB671F680370CA2572EC000DF08D?OpenDocument

21 In considering the costs and benefits associated with these options, it was noted that although the introduction of a licensing regime would provide a better balance between initial registration requirements and ongoing requirements, the costs associated may well outweigh the benefits. Concerns were raised at the time about the costs associated with greater ASIC surveillance obligations, plus additional compliance costs for practitioners that might be passed on to creditors by way of increased practitioner fees.

22 The option of targeted amendments to the existing registration regime was seen as being an appropriate response to the issues raised through consultation to improve the efficiency and cost-effectiveness of insolvency proceedings without introducing transitional costs or new compliance obligations. The 2007 Amendments, therefore, were seen as the best way to address the concerns raised by stakeholders, impose minimal new burdens on insolvency practitioners, enhance practitioner accountability, improve the supervisory framework administered by ASIC, and enhance the capacity of creditors to choose independent administrators, without incurring new budgetary costs. We have sought to administer the laws in accordance with the policy decisions that were set out in the regulation impact statement accompanying this legislation.

Conditions on registration of auditors

23 As part of the CLERP 9 amendments, s1289A was introduced, enabling ASIC to impose conditions on an auditor's registration. Details of our auditor registration requirements are outlined in Regulatory Guide 180 *Auditor registration* (RG 180). This regulatory model combines elements of both a registration regime and a licensing regime.

24 Section 1289A provides that ASIC may impose conditions on the registration of an auditor, where those conditions relate to:[2]

(a) the minimum amount and nature of continuing or other professional education that must be undertaken by a registered company auditor;

(b) the period or other review of the audit and audit-related work of a registered company auditor as part of a quality assurance or review program;

(c) having a current policy of professional indemnity insurance for claims against a registered company auditor in relation to audits conducted under the Corporations Act; and

(d) establishing and maintaining a system for resolving complaints made against a registered company auditor by audit clients in relation to audits conducted under the Corporations Act.

[2] These specific areas to which ASIC may impose a condition are detailed in reg 9.2.08 of the Corporations Regulations 2001.

25 We are not able to impose a condition outside of these areas on an individual auditor. However, we may also impose conditions on the registration of an authorised audit company.

26 We have imposed standard registration conditions on all applications for registered company auditors (RCA) since 1 July 2004. The standard conditions imposed are:

(a) professional development:

> You must document and complete a specified level of continuing professional development.

(b) professional indemnity insurance:

> You must maintain a specified level of professional indemnity insurance.

(c) quality assurance procedures:

> You must document, maintain and follow quality assurance procedures required by the Australian Auditing Standard AUS206, *Quality control for audits of historical financial information*.

(d) Complaints-handling procedures:

> You must document, maintain and follow procedures dealing with complaints by audit clients. Because the nature, scale and complexity of an RCA's businesses may vary, the compliance measures, processes and procedures you need to adopt for quality assurance and complaints will vary according to your business. However, your complaints-handling procedures should be consistent with Australian Standard AS4269:1995, *Complaints handling*.

27 We may impose additional conditions, or vary or revoke existing conditions, if an RCA was already registered before 1 July 2004. We may do this to address concerns about the conduct of a particular RCA, or RCAs generally. If we intend to impose additional conditions on an RCA (or vary or revoke existing conditions), we will first give the person the opportunity to appear before (or be represented at) a private hearing and to make submissions on the matter.

28 Imposing conditions on RCAs fosters a 'level playing field' between RCAs who are subject to the rules of a professional accounting body and those who are not. There are also additional rules that apply to authorised audit companies.

29 Below is an estimate of the additional resources required to introduce a registration regime for insolvency practitioners similar to the regime for auditors.

Estimated resources required	Start-up FTEs	Ongoing FTEs
To introduce a liquidator registration regime with the ability to impose conditions upon registration	4	1.5

Note: Detailed costings associated with this estimate are contained in confidential Appendix 4.

Proposed licence renewal period

30 The public hearings also raised the suggestion of a licensing process for liquidators, with an associated renewal period.

31 There are additional resources required with such a process, assuming that it would involve a reassessment of the licensee's ability to hold a licence to operate as a liquidator. Based on the current population of 662 registered liquidators, and assuming a three-year renewal cycle for any proposed licensing arrangement, this would involve approximately 220 licence reassessment procedures each year.

32 We envisage such a process would require the lodgement of supporting information from the liquidator, as well as an assessment by ASIC of the conduct of the liquidator over the previous period. The outcome of the assessment may result in the licence being reissued, in conditions being imposed on the licence, or in the licence being revoked or suspended. Of course, any action to revoke a licence may generally be appealed and that may in turn delay the final outcome of the relicensing process.

33 Below is an estimate of the additional resources that may be required to introduce a licensing regime with renewal requirements as set out above.

Estimated resources required	Start-up FTEs	Ongoing FTEs
To introduce a licence renewal process	2	7.06

Note: Detailed costings associated with this estimate are contained in confidential Appendix 4.

Current liquidator registration process: Introduction of interview panel

***Key issue**: Should ASIC's existing processes for the registration of insolvency practitioners include an interview with the applicant as part of the registration process?*

34 As noted during our evidence at the public hearing, we will consider, as part of our review of Regulatory Guide 186 *External administration: Liquidator registration* (RG 186), the use of an 'interview process' to be included in our existing registration procedures. Such an addition to our processes would provide an opportunity for face-to-face discussion of an application and of any resulting queries.

35 We will consult on how this process could be implemented—whether it is conducted by way of a panel of interviewers, who should be represented on the panel, and how the panel would be constituted.

36 The resources expected to be required for this process are estimated below.

Estimated resources required	Start-up FTEs	Ongoing FTEs
To introduce an interview panel into the existing liquidator registration process	1	0.14

Note: Detailed costings associated with this estimate are contained in confidential Appendix 4.

Broadening the base of practitioners

***Key issue**: Should the range of professionals who may be registered or licensed as an insolvency practitioner be extended to include professionals other than just accountants?*

37 The eligibility criteria for registration as a liquidator was broadened when ASIC issued RG 186 in September 2005, by providing flexibility in complying with the requirement to be a member of an accounting body. This idea was also subsequently supported by law reform repealing s1282(a)(1) that focused on specific membership of an accounting body.

38 We do not object to the concept of broadening the base for professionals who may practise in the insolvency industry if strong standards of conduct, experience and continuing professional development are maintained.

Professional indemnity insurance

***Key issue**: The key concerns with professional indemnity cover are the lack of redress available to claimants where a policy is cancelled (e.g. for non-payment of a premium), and the limitations associated with run-off cover and fidelity insurance for sole practitioners.*

Background

39 As part of the 2007 Amendments, requirements that registered liquidators maintain a security deposit with ASIC (via insurance performance bonds) were removed since those products were no longer available in the market. Instead, the law was amended to require that registered liquidators obtain and maintain professional indemnity insurance and fidelity insurance to cover their work as licensed practitioners.

40 The underlying policy objective of professional indemnity insurance requirements is to ensure, as far as possible, that funds are available to a registered liquidator to compensate creditors and other claimants for loss suffered as a result of the inadequate or improper performance of duties or other legal obligations by the registered liquidator in connection with externally administered companies. However, the ability of professional indemnity insurance and fidelity insurance to protect creditors and other claimants against financial loss is subject to inherent practical limitations.

41 The insurance requirements are not a mechanism for providing compensation directly to creditors or other claimants. Rather, they are a means for reducing the risk that a registered liquidator cannot meet claims arising from work performed in connection with externally administered companies because of their own insufficient available financial resources.

Basis for claims

42 A typical professional indemnity insurance policy is a 'claims made' policy. This means that cover is only provided for claims made against the insured and notified to the insurer during the period of insurance (or any extended reporting period). Claims can be made even though these may arise from acts, errors or omissions that occurred before the inception of the policy, as long as they took place on or after the policy's retroactive date, if it has one.

43 If a circumstance occurred prior to but is not notified until after the policy has expired or is cancelled, the policy will generally not cover the claim unless run-off cover is available. The key concern is that claimants are, therefore, not afforded this line of redress against the insolvency practitioner.

44 Annual professional indemnity and fidelity insurance policies also do not indemnify a registered liquidator for losses caused by their dishonest conduct or fraud if they are a sole practitioner. This is because fidelity insurance proper only indemnifies innocent parties. It does not cover any persons committing or condoning the dishonest or fraudulent act, error or omission. However, if the fraudulent or dishonest registered liquidator is insured as part of a firm, creditors can generally claim against the firm and, as an innocent insured party, the firm can be indemnified under the fidelity insurance policy.

Run-off cover

45 In relation to run-off cover, Regulatory Guide 194 *Insurance requirements for registered liquidators* (RG 194) requires two forms of run-off cover (subject to market availability):

(a) 'automatic' run-off cover—that is, cover that automatically comes into place when a firm becomes insolvent, which enables claims to continue to be made after this occurs; and

(b) 'regular' run-off cover—that is, cover that is negotiated between the policy holder and the insurer prior to the policy holder ceasing to practice in the ordinary course (e.g. when the policy holder retires from business).

46 ASIC's policy allows for a transition period so that registered liquidators are only required to include automatic run-off cover in their insurance policies when they were entered into, renewed, varied or extended on or after 1 August 2010. This transition period was considered at the time of the

initial release of RG 194 in 2008, recognising the potential limitations to access run-off cover in the insurance market.

47 Similar requirements for run-off cover exist for AFS licensees. However, recently we became aware that the high number of claims by licensees had made it unviable for insurers to offer automatic run-off cover. As a result, in October 2009, we revised our policy position, removing the requirement for these licensees to hold automatic run-off cover. It is presently unclear whether similar problems will arise for insolvency practitioners. As part of our forward program, we are undertaking an insurance project to test compliance with RG 194 by all liquidators.

ASIC initiatives

48 By December 2010 we will have requested all registered liquidators to confirm that their insurance arrangements are in place and to provide evidence of their compliance with the legislative requirements and with RG 194. In instances of non-compliance, we may cancel their registration under s1290A. We will also consider amending RG 194 to facilitate the notification to ASIC, by the insurers, of policy cancellations and non-renewals.

49 We have recently instigated discussions with the Insolvency Practitioners Association of Australia (IPA) specifically in relation to how the profession can work with insurance providers to address the following concerns:

(a) non-renewal of policy/cancellation of policy—whether underwriters/insurers would notify ASIC directly of policy non-renewals/cancellations, if requested to do so by the insolvency practitioner;

(b) 'run-off'—the possibility of policies being issued on an 'occurrence' basis rather than a 'claims made' basis, and consideration of whether an 'event' that occurred prior to the expiration of a policy for which a claim is not made until after expiration of the policy has a different standing to an 'event' that occurs after expiration of the policy; and

(c) sole practitioners—whether fidelity policies can be worded to provide indemnity to third parties where there is misconduct by the sole practitioner.

50 We will continue to work with the IPA and the insurance industry to seek resolutions of these concerns.

Improving oversight

Increasing ASIC surveillance

***Key issue**: Should ASIC's ongoing monitoring of the conduct of insolvency practitioners be stronger?*

51 We are undertaking a wide range of activities to increase and focus our resources on particular areas of concern with the insolvency industry. Specifically, paragraphs 53–58 give a more detailed outline of the outcomes expected from our projects in relation to:

(a) remuneration: approval compliance and surveillance; and

(b) independence: oversight and surveillance.

52 Additionally, we have increased the level of practitioner surveillance visits completed. In line with increasing our 'coverage' of the liquidator population, we provide an outline of the estimated additional resources required to increase our surveillance practice visits to either an annual or biennial basis.

ASIC's forward program

53 We are undertaking two key projects in relation to the remuneration and independence of insolvency practitioners: *Remuneration: Approval compliance and surveillance project* (Remuneration project), and *Independence: Oversight and surveillance project* (Independence project).

54 Under both of these projects, we are testing the implementation of the laws introduced under the 2007 Amendments that require creditors to be provided with better information to assist them in deciding whether to remove a practitioner and to decide whether remuneration is reasonable and should be approved by them.

55 The Remuneration project includes consultation on what further information and disclosures should be made to relevant stakeholders to increase the level of informed approval decisions. We may also consult and obtain industry feedback on the appropriateness of using 'cost assessors' as an alternative for stakeholders to help assess 'reasonableness' of remuneration as part of the fee approval process.

56 Key anticipated outcomes of this project are to:

(a) test the new system of disclosure;

(b) assess alternative approaches for the independent review of remuneration;

(c) examine the role of creditors' committees of inspection, and their level of engagement and understanding of their rights and responsibilities;

(d) assess what further guidance we should issue given the application of the new laws;

(e) work with the industry body (IPA) to improve industry guidance as a result of our findings; and

(f) establish a platform for ASIC deterrence action.

57 As part of the Independence project, we are consulting on independence issues.

58 Key anticipated outcomes of this project are to:

(a) test the application of the new law;

(b) raise industry standards through greater awareness and consistency of application;

(c) assess what further guidance we should issue given the application of the new laws;

(d) work with the industry body (IPA) to improve industry guidance as a result of our findings; and

(e) establish a platform for ASIC deterrence action.

ASIC's surveillance approach

59 During the public hearings, comment was made as to the surveillance approach adopted by ITSA compared with that undertaken by ASIC. To assist the Inquiry, Table 5 sets out a comparison of the two approaches.

Table 5: Comparison of surveillance methodology of ASIC and ITSA

Element	ASIC (Practice Compliance Reviews)	ITSA* (Trustee Inspections)
Approach	Risk-based	Annual inspection (aim to inspect entire population annually)
Regulated population	662 registered liquidators	309 trustees** 57 debt administrators**
Individual surveillance resources	Two FTEs over 3–4 weeks per review (due to complexity of corporate insolvency)	Not publicly available
Number of files inspected per surveillance visit	Approximately 10	Not publicly available

Element	ASIC (Practice Compliance Reviews)	ITSA* (Trustee Inspections)
Areas of review	Compliance with legislation and common law requirements Proper performance of statutory and fiduciary duties—focus on independence, reporting (both statutory and creditor obligations), remuneration, asset realisation decisions and conduct of meetings Financial records, billing and money-handling practices System and control weaknesses—internal procedures and checklists	Compliance with legislation and common law requirements Proper performance of statutory and fiduciary duties Financial records, billing and money-handling practices Systems and control weaknesses
Outcomes	Review outcomes may include: • consideration of matter for referral to CALDB or for further deterrence action (either civil or criminal) • consideration of appropriateness of an enforceable undertaking • informal rectification of minor concerns, with an undertaking for further follow up/subsequent reporting	Inspection outcomes are categorised as: • Category A—very serious errors or breaches requiring immediate attention by the trustee • Category B—serious or systemic errors • Category C—one-off or minor practice or procedural errors

* Information sourced from ITSA's website.

** Information sourced from ITSA *Hansard* evidence, 13 April 2010.

60 As noted in our first submission, we are in the process of undertaking 10 high-risk practice compliance reviews by December 2010 in addition to our ongoing work in dealing with serious complaints and major project work.

61 Since July 2006 our insolvency team has undertaken a total of 163 transaction assessments/reviews and 16 practice compliance reviews—179 matters in total, including the 78 complaint referrals from ASIC's Misconduct and Breach Reporting team. In 21% of the 179 reviews, the conduct or concern in question was remedied voluntarily by the insolvency practitioner, and in 8% of reviews the alleged misconduct was referred on for further deterrence work.

62 Presently, the insolvency team includes a group of 31 staff, which provides the team with the ability to focus resources on serious instances of misconduct on a timely basis—whether this be misconduct by an insolvency practitioner or an instance of alleged misconduct as to an entity that may be trading while insolvent. This team, as noted in our first submission, undertakes a wide range of activities, including inquiries as to instances of liquidator misconduct.

63 Although the existing risk-based approach does not ensure that each practitioner is visited within a specified period, the approach is an efficient allocation and use of resources.

64 All other ASIC stakeholder team surveillance programs are similarly based on a risk assessment of the entity, which then determines the level of regulatory interaction that we have with them. If we change our surveillance approach specifically for insolvency practitioners, we would need to consider whether this would have impacts on other surveillance programs that we conduct.

65 In order for ASIC to obtain a similar level of monitoring of registered liquidators to that of the ITSA surveillance model (i.e. either with the aim to review each liquidator on an annual or biennial basis), we estimate we would require an additional:

(a) 65 FTEs if we undertook to visit each liquidator annually; or

(b) 31 FTEs if we undertook to visit each liquidator on a biennial basis.

Estimated resources required	Start-up FTEs	Ongoing FTEs
To increase surveillance frequency and coverage over the entire registered liquidator population[3]	—	'Annual' surveillance approach: 65 FTEs 'Biennial' surveillance approach: 31 FTEs

Note: Detailed costings associated with this estimate are contained in confidential Appendix 4.

Penalties

***Key issue**: Are penalties for liquidator misconduct strong enough?*

66 Below is an outline of the current penalty provisions for liquidator misconduct, which are in addition to the range of deterrence outcomes available to ASIC and as outlined in our first submission (e.g. CALDB, court remedies).

67 We consider there may be a case for review of some of these penalties given the important 'gatekeeper' role that insolvency practitioners have.

Existing penalties for insolvency practitioner misconduct

68 The penalty provisions of the Corporations Act focus on liquidator misconduct via the cancellation or suspension of registration under Div 3, Pt 9.2. Additionally, the court has the power to inquire as to the conduct of liquidations and administrations under s447E and 536.

[3] Given the internal nature of the focus or surveillance approach adopted, there are no significant start-up FTEs associated; hence, the analysis undertaken has categorised the FTEs associated with the surveillance approach as being ongoing costs.

69 A liquidator can, however, be liable for penalties under s1311 of the Corporations Act (general penalty provisions), given their role as an officer of the company. Additionally, Sch 3 of the Corporations Act sets out specific penalties associated with certain offences:

(a) s448B(1)—administrator must be a registered liquidator: this is a strict liability offence with 25 penalty units or imprisonment for 6 months or both (i.e. $2750);

(b) s448C—an administrator must not be 'connected' with the company: this is a strict liability offence with 25 penalty units or imprisonment for 6 months or both (i.e. $2750);

(c) s448D—an administrator must not be an 'insolvent under administration': this is a strict liability offence with penalty units or imprisonment for 6 months or both (i.e. $2750); and

(d) s532—circumstances where a liquidator must not consent to act: this is a strict liability offence with 10 penalty units or imprisonment for 3 months or both (i.e. $1100).

Note: A penalty unit is defined under s4AA of the *Crimes Act 1914*, and is presently set at $110 per penalty unit.

70 These penalties are in addition to the range of deterrence outcomes that are available to ASIC, as outlined in our first submission, for insolvency practitioner misconduct.

Role of an industry ombudsman

***Key issue**: Should an insolvency ombudsman be created to provide an independent, efficient and timely mechanism for the resolution of creditor and other stakeholder concerns with liquidator conduct?*

71 One of the key issues raised during the hearings was the possible introduction of an independent dispute resolution scheme, such as an ombudsman, to resolve disputes between stakeholders and insolvency practitioners. However, it is important to note that there are a range of models to provide dispute resolution to consumers, rather than just the appointment of an ombudsman.

72 The Australia and New Zealand Ombudsman Association highlights that an ombudsman service should have six key features:

- independence—independent from the organisations being investigated;
- jurisdiction—jurisdiction should be clearly defined;
- powers—must have appropriate powers to investigate, collect information, initiate actions and to have the discretion to choose the most appropriate procedure for dealing with the complaint;

- accessibility—a complainant must be able to directly approach the ombudsman for no charge;
- procedural fairness—the procedures that govern the investigation work must embody a commitment to the requirements of procedural fairness; and
- accountability—if an industry-based ombudsman, must be responsible to an independent board of industry and consumer representatives.

73 A key function of such an ombudsman service is dispute resolution. This function can be provided by an ombudsman where there are no other dispute resolution avenues available. Alternatively, dispute resolution mechanisms can be provided as part of a licensing regime.

74 As we have noted earlier, as part of the existing licensing regime for financial service providers, the licensee is required to not only have IDR procedures, but to also be a member of an EDR scheme.

75 We have provided a brief outline of the dispute resolution requirements for AFS licensees under the Corporations Act. We are responsible for overseeing the effective operation of EDR schemes in the financial services industry and approving these schemes as required. The dispute resolution requirements under the financial services regime are summarised at Table 6.

Table 6: Dispute resolution requirements under the Corporations Act

Requirements	Details	Reference
General	AFS licensees must have a dispute resolution system that covers complaints by retail clients. It must consist of: • an IDR procedure that complies with standards and requirements made or approved by ASIC; and • membership of one or more ASIC-approved EDR schemes	See s912A(1)(g), 912A(2) and 1017G of the Corporations Act
IDR procedure	When considering whether to make or approve standards or requirements relating to IDR procedures, we must take into account: • Complaints handling standard AS ISO 10002-2006; and • any other matter we consider relevant.	See reg 7.6.02(1) and 7.9.77(1)(a) of the Corporations Regulations 2001 and ASIC's requirements set out in Regulatory Guide 165 *Licensing: Internal and external dispute resolution* (RG 165)

Requirements	Details	Reference
EDR schemes	AFS licensees must have a system for informing complainants about their right to complain to an EDR scheme. We have the power to approve, vary or revoke the approval of an EDR scheme. When approving a scheme, we must take into account: • the accessibility of the scheme • the independence of the scheme • the fairness of the scheme • the accountability of the scheme • the efficiency of the scheme • the effectiveness of the scheme • any other matter we consider relevant.	See reg 7.6.02(3) and 7.9.77(3) of the Corporations Regulations 2001 See our Regulatory Guide 139 *Approval and oversight of external dispute resolution schemes* (RG 139), which explains how EDR schemes can obtain initial approval and, once approved, their ongoing requirements to maintain their ASIC approval

IDR procedures

76 In the context of financial services, our view is that the majority of complaints are dealt with under IDR procedures and therefore it is essential for an AFS licensee to have effective IDR procedures in place so that complaints are dealt with genuinely, promptly, fairly and consistently: see RG 165. Independent research commissioned by ASIC in relation to the AFS regime indicates that timely resolution of complaints, particularly by IDR, can be instrumental in consumers and investors being satisfied with the complaints-handling process.[4]

77 There may be merit in considering the introduction of IDR requirements for insolvency practitioners because it is often the most efficient and cost-effective way to deal with complaints. However, any proposal would require comprehensive industry consultation. We are mindful that the role of an insolvency practitioner results in close public scrutiny. The insolvency practitioner is usually trying to allocate insufficient funds to a range of people who might not understand why they are to receive less than 100 cents in the dollar. Therefore, imposing a requirement for insolvency practitioners to have an IDR scheme may result in significant burdens on an insolvency practitioner. It is likely that the additional resources and costs required to implement and maintain an IDR scheme will be passed on to stakeholders by way of increased fees.

EDR procedures

78 Advocates for the introduction of EDR schemes believe that they are quicker and cheaper than the legal system. An EDR also offers the opportunity to improve industry standards of conduct and it will improve relationships

[4] See paragraphs 15–21 of Consultation Paper 102 *Dispute resolution: Review of RG 139 and RG 165* (CP 102).

between insolvency practitioners and stakeholders because it is less adversarial.

79 An EDR scheme will normally hear a complaint for free. So the cost of implementing and maintaining any scheme would likely be borne by insolvency practitioners. However, it is likely that these costs will be passed on to stakeholders via increased fees for an external administration. This cost consideration is particularly significant in light of the contested nature of insolvency work and the anecdotal evidence that a number of stakeholders may avail themselves of the dispute resolution process. Additional resources would also be needed for regulators to implement any reform. An alternative option that might not require law reform would be to work with the IPA to see what additional role they would be willing to play in resolving disputes involving their members.

Oversight of directors in SMEs

***Key issue**: The fraudulent use of company structures (i.e. phoenix company activity).*

80 See confidential Appendix 4, which provides an outline of our submission to the recent Treasury proposals paper, *Action against fraudulent phoenix activity*. We have included this material as part of the confidential appendix, as this material was originally provided to Treasury on a confidential basis.

Key terms

Term	Meaning in this document
2007 Amendments	Corporations Amendment (Insolvency) Bill 2007
AAT	Administrative Appeals Tribunal
AFS licensee	Australian financial services licensee
ASIC	Australian Securities and Investments Commission
CALDB	Companies Auditors and Liquidators Disciplinary Board—the independent statutory body that considers applications from ASIC and APRA regarding the conduct of registered auditors and liquidators
CLERP 9	*Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2003*
Corporations Act	*Corporations Act 2001*, including regulations made for the purposes of that Act
Corporations Regulations	Corporations Regulations 2001
creditor	A person who is owed money
Deterrence or Deterrence team	ASIC has eight Financial Economy Deterrence teams, each with specific areas of focus. Deterrence teams deal with cases that seek to have a deterrent effect, or drive a behavioural change, in their relevant industry or area.
DOCA	Deed of company arrangement
EDR	External dispute resolution
enforceable undertaking	One of the remedies available for breaches of the legislation as an alternative to civil or administrative action
external administration	The corporate insolvency that the external administrator has been appointed to administer
external administrator	A general term for an external person formally appointed to a company or its property. Includes provisional liquidator, liquidator, voluntary administrator, deed administrator, controller, receiver, and receiver and manager. Other than a liquidator for a members' voluntary liquidation and a controller who is not a receiver or receiver and manager, an external administrator is required to be registered by ASIC. An external administrator is sometimes also referred to as an insolvency practitioner
FOS	Financial Ombudsman Service
FTE	Full-time equivalent
IDR	Internal dispute resolution

Term	Meaning in this document
IPA	Insolvency Practitioners Association of Australia, the leading professional organisation in Australia for external administrators/insolvency practitioners.
ITSA	Insolvency and Trustee Service of Australia
liquidation	The orderly winding up of a company's affairs. It involves realising the company's assets, cessation or sale of its operations, distributing the proceeds of realisation among its creditors and distributing any surplus among its shareholders. The three types of liquidation are: court, creditors' voluntary and members' voluntary
liquidator	An external administrator appointed to undertake the liquidation of a company
official liquidator	An external administrator appointed by a court to undertake the liquidation of a company
provisional liquidator	An official liquidator appointed by the court to preserve a company's assets until a winding-up application is decided
RCA	Registered company auditors
receiver	An external administrator appointed by a secured creditor to realise enough of the assets subject to the secured creditor's charge to repay the secured debt. Less commonly, a receiver may also be appointed by a court to protect the company's assets or to carry out specific tasks
receiver and manager	A receiver who has, under the terms of their appointment, the power to manage the company's affairs
registered liquidator	A person registered by ASIC under s1282(2) of the Corporations Act
regulatory guide	A document issued by ASIC to explain when and how ASIC will exercise its powers , including how it will interpret the law, also giving practical guidance
RG 194 (for example)	An ASIC regulatory guide (in this example numbered 194)
s1289A (for example)	A section of the Corporations Act (in this example numbered 1289A), unless otherwise specified
secured creditor	A creditor who has a security (e.g. charge or mortgage) over some or all of a company's property
SME	Small-to-medium enterprise
unsecured creditor	A creditor who does not hold a security over a company's property
voluntary administrator	An external administrator appointed to carry out the voluntary administration of a company

Appendix 1: Related information—Additional terms of reference: Receivers

Key points

This appendix provides an outline of the regulatory environment and ASIC activities as they relate to receivers, as if receivers had been included in the original terms of reference of the Inquiry.

Environment and regulatory framework

Primary purpose

81 A company goes into receivership when a receiver[5] is appointed by a secured creditor,[6] or in special circumstances by the court, to take control over some or all of the company's assets. The function of most receiverships is for the receiver to collect and sell sufficient of the company's charged assets to repay the debt owed to the secured creditor. Less commonly, a receiver may be appointed by a court to protect the company's assets or to carry out specific tasks.

Basis for appointment

82 A receiver can be appointed by a court or by a private appointee.

Private appointment

83 A private appointment can be made by anyone with the contractual power to do so. Most commonly, a private appointment is made pursuant to an express agreement between the parties with an interest in the property over which the appointment is made (e.g. under the terms of a mortgage or debenture). The mortgage, debenture or other agreement will usually set out preconditions or events which may give rise to the power to appoint a receiver. The conditions are usually events that indicate that a party's interest is likely to be prejudiced, such as a default in repayment.

84 A private appointment may also be made following a statutory power of appointment.[7]

[5] For the purposes of this submission, unless the contrary intention appears, we have used the term 'receiver' to include a 'receiver and manager', 'controller' and 'managing controller'. See paragraphs 92–95 for the definitions of these terms.
[6] A secured creditor is someone who has a charge, such as a mortgage, over some or all of the company's assets, to secure a debt owed by the company. An unsecured creditor is a creditor who does not have a charge over the company's assets.
[7] For example, s115A of the *Conveyancing Act 1919* (NSW) allows a mortgagee under a mortgage to appoint a receiver if the default has been made in respect of the mortgage.

85 It is possible for a company in receivership to also be in provisional liquidation, liquidation, voluntary administration or subject to a deed of company arrangement. A receiver can be appointed to a company in liquidation or under any other form of external administration. A receiver can be appointed to a company in voluntary administration with the consent of the court or the administrator, where the consent is provided within the first 13 business days of the appointment of an administrator and where the charge, under which the receiver is being appointed, is over substantially the whole of the assets of the company.[8] In most cases the appointment of an external administrator is a trigger for the appointment of a receiver.

Court appointment

86 The court has an inherent jurisdiction to appoint a receiver. This inherent power has been restated in various statutes.[9] The court also has power under the Corporations Act to appoint a receiver. For example, the court may appoint a receiver upon the application of an aggrieved person[10] or upon the application of a liquidator or provisional liquidator in the circumstances where an officer of the company in liquidation, or of a related entity of the company, may otherwise avoid liability to the company in liquidation.[11]

87 The powers of a court-appointed receiver will be expressed in the court order and will be specific to the facts giving rise to the application and be supported with powers under the Corporations Act.

Landscape

88 Appointments of receivers, receivers and managers, and controllers account for a relatively small percentage of the total number of annual insolvency practitioner appointments.

89 For the period July 2008–June 2009, receiver/receiver and manager appointments accounted for 11% and controllers accounted for 6% of all external administration appointments.

90 Further detail on the appointments of receivers is provided in Appendix 2.

Types of 'receiver' appointments

91 There are a number of different types of appointments in this area: receivers, receivers and managers, controllers, and managing controllers.

---

[8] Refer to s441A—a charge with a charge over substantially all the assets can appoint during the 'decision period' (refer to s9 for the definition of 'decision period').
[9] For example, s67 of the *Supreme Court Act 1970* (NSW) and s62(2) of the *Supreme Court Act 1958* (Vic).
[10] Section 1323(1) of the Corporations Act.
[11] Section 486A of the Corporations Act.

Receiver

92 A receiver is appointed to administer property. The appointment may be limited to mere protection of one particular item of property or it may extend to managing the affairs of the company. The term 'receiver' is defined to include a receiver and manager under Part 5.2 of the Corporations Act.[12]

Receiver and manager

93 A receiver and manager is a receiver who has, under the terms of their appointment, the power to manage the company's affairs.[13]

Controller

94 A controller is defined as a receiver, receiver and manager, or any other controller who has entered into possession or control of the corporation's property for the purposes of enforcing a charge.[14]

Managing controller

95 A managing controller is a receiver and manager or any other controller who has entered into possession or control, but additionally has functions or powers in connection with managing the company.[15]

96 The statistics for controller and receiver appointments for the 2006–07 financial year through to December 2009 are shown in Table A1.1.

Table A1.1: Companies entering receiver appointments[16]

Type of external administration	2006–07	2007–08	2008–09	Jul–Dec 2009	Total
Receiver or receiver and manager	309	400	829	409	1,947
Controller of managing controller	137	206	415	266	1,024
Total	**446**	**606**	**1,244**	**675**	**2,971**

Source: ASIC insolvency statistics—Companies entering external administration

Registration framework

97 The Corporations Act provides that a receiver must be a registered liquidator.[17] A court-appointed receiver must be registered as an official liquidator.

[12] Section 416 of the Corporations Act.
[13] Section 90 of the Corporations Act.
[14] Section 9 of the Corporations Act.
[15] Ibid.
[16] Members' voluntary liquidations are not included as the companies are not insolvent.
[17] Section 418(1)(d) of the Corporations Act.

98 The requirements for a liquidator to be registered with ASIC were outlined in ASIC's first submission to the Inquiry (dated March 2010) at paragraphs 14–16 and Appendix B4. These requirements also apply to a receiver. However, in addition to those requirements, the Corporations Act provides that certain persons are excluded from acting as a receiver. For example, a person cannot be appointed as a receiver if they are a mortgagee of the property of the corporation, or an auditor or a director, secretary, senior manager or employee of the corporation.[18]

Obligations of receivers

99 The conduct obligations imposed on a receiver are derived from a number of sources. A receiver is subject to requirements under the Corporations Act and general law as well as ASIC regulatory guidance explaining, among other things, when and how ASIC will exercise specific powers under the legislation and how ASIC interprets the law. Receivers who are members of a professional body (e.g. the IPA and/or professional accounting bodies) will also be subject to the professional conduct standards of that body.

General law duties

100 At general law, a receiver owes a duty to the secured creditor and the company. These duties are derived from:

(a) the agreement under which the receiver was appointed;

(b) the agency relationship with the company (or more rarely with the secured creditor); if the receiver is court-appointed, from being an officer of the court; and

(c) being an officer of the company.

Privately appointed receiver

101 The fundamental duty of a privately appointed receiver is to exercise their powers bona fide for the purposes for which they were appointed and, therefore, a receiver's primary duty is to the secured creditor.

102 The receiver will also be subject to general law duties to the company as a consequence of the agency relationship that arises from the terms of the agreement. While the receiver is acting for the secured creditor, the agreement will invariably provide that the receiver will be the agent of the company rather than the secured creditor. This is to ensure that the secured creditor is not liable as the receiver's principal and as mortgagee in possession. This agency relationship ceases if a liquidator is appointed, although there is an opportunity to continue if the liquidator consents.

[18] Section 418 of the Corporations Act.

103 As an agent of the company, the receiver has certain duties to the company which are directly enforceable by the company. Australian case law indicates that these duties include a duty to:

(a) exercise his or her powers in good faith (including a duty not to sacrifice the company's interests);

(b) act strictly within, and in accordance with, the conditions of his or her appointment; and

(c) account to the company after discharging the secured creditor's security, not only for the surplus assets, but also for his or her conduct of the receivership (including the duty to terminate the receivership as soon as the interests of the secured creditor have been satisfied).[19]

Court-appointed receiver

104 The nature of the powers endowed on a receiver is determined by the order of the court.

105 Unlike a privately appointed receiver, it is not the fundamental function of a court-appointed receiver to see that the security holder is repaid. As an officer of the court, the appointment is for the benefit of those interested in the relevant assets.[20] For example, a court-appointed receiver may be appointed to preserve property pending the hearing or resolution of the dispute, as opposed to a privately appointed receiver whose role it is to realise the secured assets.

Corporations Act

106 The Corporations Act deals with the qualifications of a receiver and imposes a number of specific duties on receivers. These requirements apply equally to a privately appointed receiver and a court-appointed receiver. For example, a receiver is required to:

(a) lodge a notice of appointment with ASIC within 14 days of appointment;

(b) take all reasonable care to sell the property of the corporation for not less than market value or the best price that is reasonably obtainable;

(c) open and maintain a bank account, and deposit into this account all money of the company which comes under the receiver's control;

(d) keep financial records that correctly record and explain all transactions that the receiver enters into as a receiver of the company and permit access by any director, creditor or member to records kept;

---

[19] *Expo International Pty Ltd (Recs and Mgrs Apptd) (in liq) & Another* v *Chant & Others* [1979] 2 NSWLR 820 per Needham J at 834.
[20] *Cape v Redarb Pty Ltd (Rec and Mgr Apptd)* (1992) 107 FLR 362.

(e) lodge six-monthly accounts of receipts and payments with ASIC;

(f) pay certain debts in priority to repayment of debts that are secured by a floating charge;

(g) prepare and lodge a report with ASIC on the affairs of the company within two months of being appointed if the receiver is managing the company; and

(h) report any possible misconduct to ASIC.

107 These obligations provide a level of protection for stakeholders, such as unsecured creditors and members of the company, and accountability through the reporting and lodgement requirements with ASIC. It should be noted, however, that receivers have no obligation to report directly to unsecured creditors.

108 It should also be noted that a person appointed as a controller or managing controller does not have to comply with the requirement for independence and a receiver does not have to provide creditors with a Declaration of Independence, Relevant Relationships and Indemnities. This is in accordance with the law that requires these types of declarations to be made only in voluntary administrations and creditors' voluntary liquidations.

Duties as an 'officer'

109 An 'officer' is defined in the Corporations Act to include a receiver.[21] The general duties that apply to 'officers' of a corporation will therefore apply to receivers, in particular those duties under Ch 2D of the Corporations Act:

(a) to act in good faith at all times;

(b) to exercise a reasonable degree of care and diligence;

(c) not to make improper use of information; and

(d) not to make improper use of position.

ASIC's regulatory guidance

110 We have issued the following regulatory guides to assist receivers to understand their obligations under the Corporations Act:

(a) Regulatory Guide 14 *Receivers: Retention of company records* (RG 14); and

(b) Regulatory Guide 106 *Controller duties and bank accounts* (RG 106).

[21] Section 9 of the Corporations Act.

111 We have also issued two information sheets to assist stakeholders to understand the process of receivership and the implications for the particular stakeholder, namely:

(a) Information Sheet 54 *Receivership: a guide for creditors* (INFO 54); and

(b) Information Sheet 55 *Receivership: a guide for employees* (INFO 55).

Professional conduct standards

112 A receiver will be subject to professional standards, practices and principles, including codes of conduct and statements of best practice of a relevant professional body or an insolvency industry body of which the registered liquidator is a member. These professional conduct standards are:

(a) APES 330 *Insolvency Services*, effective 1 April 2010 (replacing APS 7), issued by the Accounting Professional and Ethics Standards Board Limited; and

(b) the IPA Code of Professional Practice (the IPA Code).

113 These professional conduct standards were considered in ASIC's first submission at paragraphs 124–131.

IPA Code

114 By way of example, a receiver who is a member of the IPA must comply with IPA's professional standards, the IPA Code.

115 The IPA Code imposes various obligations on 'members' of the IPA and/or 'practitioners' as defined in the Code. Receivers, although practitioners, do not have the same fiduciary responsibilities to all creditors and therefore receivers are excluded from certain requirements of the IPA Code.

116 If a receiver breaches the IPA Code, the IPA may instigate action against them. The IPA Code is referred to by the courts when considering the required level of professional competence and conduct and consequently is also taken into account by ASIC when assessing possible contraventions of the Corporations Act.

Remuneration and disbursements

117 In the case of a private appointment, a receiver is entitled to receive such remuneration as is determined by:

(a) the debenture agreement and the document of appointment;

(b) where the appointment is made following a statutory power of appointment, the terms of that legislation;[22] or

(c) in rare cases, an express or implied agreement between the receiver and the debenture holders where he or she is acting as their agent.

118 Most commonly, the terms of the debenture agreement and the document of appointment will provide how the receiver's remuneration is to be determined, including who will approve the remuneration, the method for calculating remuneration and who is liable to pay the remuneration. Subject to the terms of the agreement, the company will usually bear the receiver's remuneration and the receiver will draw their remuneration during the course of the receivership by submitting an account for their remuneration to the secured creditor, and those costs will generally then be added to the outstanding debt of the company. This account will normally be scrutinised by and approved for payment by the secured creditor. Commonly, the receiver will secure an indemnity for remuneration and expenses from the secured creditor.

119 The secured creditor has a significant degree of influence over the level of remuneration of the receiver, due to the direct nature of the appointment. In some situations, this position can result in lower hourly rates being charged by receivers.

120 A court-appointed receiver is entitled to receive such remuneration as is determined by the court. There is no fixed or predetermined basis for calculating remuneration for a court-appointed receiver, but in attempting to set a reasonable level of remuneration the courts often accept fees charged based on hourly rates.[23]

121 We should also highlight the situation where multiple insolvency practitioners may be appointed to a company—for example, where a company may be in voluntary administration as well as having a receiver and manager appointed; or where a company is in liquidation in addition to having a receiver and manager appointed. Where a company has multiple appointments, in particular where there is a concurrent appointment of a liquidator as well as a receiver, the liquidator is entitled to an accounting in relation to the conduct of the receivership.

Approval process

122 Unlike the types of external administration considered in ASIC's first submission at paragraphs 132–150, the Corporations Act does not prescribe

[22] For example, a receiver appointed under the powers in the *Conveyancing Act 1919* (NSW) is entitled to receive (unless the mortgage deed provides otherwise) remuneration at a rate not exceeding 5% of the gross money received, or such higher rate as the court will grant on application: s115(6).
[23] *Waldron* v *MG Securities (Australasia) Ltd & Others* (1979) CLC 40–541.

the process for the approval of a receiver's remuneration, as the appointment of a receiver is essentially a private appointment.

123 The IPA Code is somewhat helpful in this regard, although it is limited in its application to members of the IPA. The IPA Code states principles and gives guidance on the remuneration of receivers. The second remuneration principle in the IPA Code requires that a claim for remuneration must provide sufficient, meaningful, open and clear disclosure to the approving body so as to allow that body to make an informed decision.

124 For court-appointed receiver, the method for applying for approval for remuneration is for the receiver to present his or her accounts and remuneration claim to the court. The approval process for the remuneration of privately appointed receivers is determined by negotiation between the parties. However, the court retains wide powers under the Corporations Act to set and review the remuneration of receivers.[24]

Rights of review

125 The Corporations Act provides for a review process regarding the remuneration payable to receivers. The court retains wide powers to set and vary the remuneration of receivers. Applications to fix or vary a receiver's remuneration may be made in certain circumstances by ASIC, a liquidator, voluntary administrator or deed administrator of the company.

126 The 2007 reforms to the Corporations Act introduced amendments that require the court, when reviewing or setting a receiver's remuneration, to have regard to whether the remuneration is reasonable, taking into account various matters, including whether the work performed was reasonably necessary.[25]

Remuneration and unsecured creditors

127 Unsecured creditors have no role in setting or approving a receiver's fees. If a liquidator is appointed to the company then the liquidator is able to review the validity of the appointment of the receiver and to monitor the progress of the receivership, including remuneration and reporting back to all unsecured creditors.

128 Often in receiverships the secured creditor suffers a significant deficit on the recovery of the debt owed by the company. In these circumstances, the unsecured creditors are not further disadvantaged by the quantum of the receiver's remuneration, as they are paid by the secured creditor.

[24] Section 425 of the Corporations Act.
[25] Section 425(8) of the Corporations Act.

Disciplinary and deterrence framework

129 The Corporations Act provides that a receiver must be a registered liquidator[26] and therefore ASIC's powers in respect of alleged misconduct by a receiver are the same as those considered for a registered liquidator in ASIC's first submission at paragraphs 151–166.

130 In summary, we may:

(a) take administrative or conduct proceedings against a receiver before CALDB;

(b) instigate court proceedings; or

(c) enter into an enforceable undertaking with the receiver.

CALDB

131 CALDB can apply penalties ranging from a reprimand to suspension or cancellation of the liquidator's registration. CALDB does not impose pecuniary penalties and is not empowered to make orders as to restitution or compensation.

Court proceedings

132 If a receiver has not faithfully performed his or her functions, ASIC may instigate court proceedings against a receiver and the court may take such action as it sees fit, including making orders for compensation or restitution.[27]

133 A receiver is also subject to a number of specific duties as a receiver and as an 'officer' under the Corporations Act. These duties were discussed at paragraphs 106–109. The penalties for breaching these provisions range from civil damages for not exercising a duty of care in disposing of property,[28] to both civil and criminal penalties for breaching the Ch 2D duties imposed on officers. The sections can all result in the application of civil penalty provisions, with compensation orders[29] and pecuniary penalty orders up to $200,000.[30] Section 184 makes it an offence for an officer, including a receiver, to be reckless or intentionally dishonest and fail to exercise their powers and discharge their duties in good faith in the best interests of the company, attracting a penalty of up to $220,000 and/or imprisonment for five years.

[26] Section 418(1)(d) of the Corporations Act.
[27] Section 423 of the Corporations Act.
[28] Section 420A of the Corporations Act.
[29] Section 1317H of the Corporations Act.
[30] Section 1317G of the Corporations Act.

International position

134 To assist the Inquiry, and noting the issues raised during the course of the public hearings, we provide some background information about the status of 'administrative receiverships' as they exist within England and Wales.

135 The *Enterprise Act 2002* (UK) (EA Act) commenced in England and Wales on 15 September 2003,[31] providing for major changes to the corporate insolvency regime in that jurisdiction. The key elements of this legislation were around:

(a) streamlining administrations;

(b) restricting the use of administrative receiverships; and

(c) abolition of Crown preference and introduction of the 'prescribed part'.

136 The EA Act therefore prohibits, subject to certain exceptions, the right to appoint an administrative receiver in all cases where a floating charge was created on or after the commencement of the provisions on 15 September 2003. This change, as well as the streamlining of the administration process, sought to promote the use of administrations more generally.

137 The exceptions created to the general abolition of administrative receiverships are aimed primarily at facilitating the proper working of capital markets or ensuring the continued operation of certain public services.[32] The exceptions are highly specific to certain large scale financial arrangements or particular entities and still permit the appointment of an administrative receiver in highly prescribed circumstances. The exceptions relate to:

(a) capital market arrangements;

(b) public–private partnerships;

(c) utilities;

(d) urban regeneration projects;

(e) project finance;

(f) financial markets;

(g) registered social landlords; and

(h) protected companies.

[31] The concept of an administrative receivership was created by the *Insolvency Act 1986* (UK) and although also subject to certain legal duties, an administrative receiver primarily owes a duty of care to the party making the appointment in seeking repayment of the debt due, and not to the general body of creditors as a whole. Concerns as to this approach were discussed in the UK Government's 2001 white paper, noting that the process was insufficiently transparent and that an administrative receiver was not accountable to stakeholders other than the charge-holder that had made the appointment. Additionally, an administrative receiver has no express duty to seek to rescue a company and there was a belief that the process may have been overused and perhaps had caused some companies to have failed unnecessarily.

[32] Any dilution of a secured creditor's rights to appoint a receiver and manager may impact on the availability of credit. However, at both a legal and commercial level there are already a number of mechanisms in the Australian regime that may reduce this risk.

138 The evaluation of the EA Act, 'Enterprise Act 2002—Corporate Insolvency Provisions: Evaluation Report, January 2008', notes that the exceptions appear to be operating as intended and are not a general loophole for the appointment of an administrative receiver in what could be termed 'normal' insolvencies.

ASIC's activities (what we are doing now)

139 In our first submission, we provided an outline of ASIC's current activities regarding insolvency practitioners. Those activities apply equally to the conduct of receivers, in particular our comments on:

(a) registration of insolvency practitioners;

(b) practitioner conduct guidance;

(c) monitoring and surveillance; and

(d) deterrence activities.

Complaints and general enquiries regarding insolvency practitioners

140 In our first submission, statistics were provided for complaints and general enquiries regarding insolvency practitioners. Those statistics and the related commentary also apply to the conduct of receivers, with complaints numbers about receiver conduct being included in the statistics on 'insolvency practitioners'.

ASIC compliance activities—Post-corporate collapse

Statutory reports

141 Receivers are required to report to ASIC as soon as practicable if it appears to the receiver that an officer may have been guilty of an offence under s422 of the Corporations Act. Additionally, under s432, they must lodge accounts with ASIC every six months.

142 Following a review, we reissued Regulatory Guide 16 *External administrators: Reporting and lodging* (RG 16) in July 2008. Initial statutory reports now request more specific detail from external administrators about alleged offences and the documentary evidence that may exist to support their allegations, helping ASIC to better target matters warranting further inquiry and the subsequent requests for supplementary reports.

143 In our first submission, we provided an outline of the number of statutory reports received and of the review that we undertook of them. The lodgement and review of reports lodged under s422 were included in those statistics.

144 The statistics specifically in relation to s422 reports are noted in Table A1.2.

Table A1.2: Statutory reports (s422) and ASIC review

	2009–10 (to Dec 2009)	2008–09	2007–08	2006–07
Total reports received	**84**	**162**	**91**	**84**
Reports assessed alleging misconduct or suspicious activity	82	161	91	84
Initial reports[33]				
Reports assessed alleging suspicious activity	58	101	60	45
Supplementary reports requested	9%	28%	35%	22%
Analysed, assessed and recorded	91%	72%	65%	78%
Supplementary reports[34]				
Supplementary reports assessed alleging misconduct	24	60	31	39
Referred for compliance, investigation or surveillance	6%	11%	9%	0%
Referred to assist existing investigation or surveillance	6%	17%	% Not captured	% Not captured
Analysed, assessed and recorded	88%	66%	91%	83%
Identified no offences	0%	6%	0%	17%

145 Of the 418 reports alleging misconduct or suspicious activity assessed by ASIC over the period, 232 refer to alleged contraventions of director duties (s180–184 of the Corporations Act) and 127 refer to alleged contraventions of s588G (being the obligation on directors to prevent the insolvent trading of the company).

ASIC's forward program for receivers (what we are doing to improve what we do now)

146 Our forward program, as outlined in our first submission, addresses the conduct of receivers through the work being undertaken on project transparency to provide complainants with clearer information on how ASIC has handled their complaint.

147 We also undertake surveillance of matters raised as a result of serious complaints made as to the conduct of receivers.

[33] Initial reports are electronic reports lodged under Schedule B of RG 16. Generally, we will determine whether to request a supplementary report on the basis of an initial report.
[34] Supplementary reports are typically detailed free-format reports, which detail the results of the external administrator's inquiries and the evidence to support the alleged offences. Generally, we can determine whether to commence a formal investigation on the basis of a supplementary report.

Appendix 2: Related information—The 'receiver' landscape

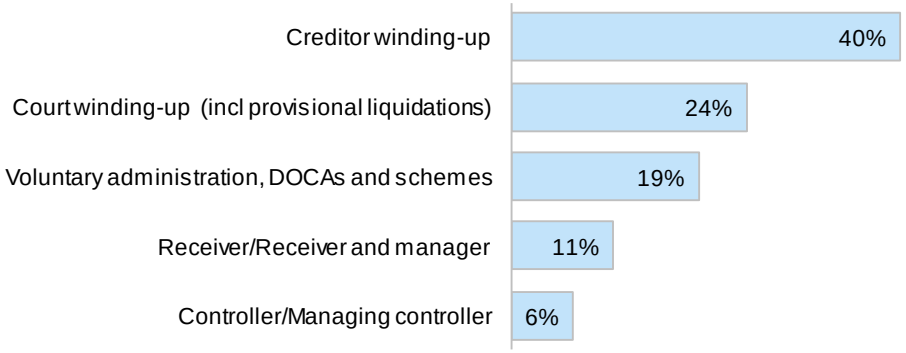
Key points

To assist the Inquiry, this appendix provides background information about the size and structure of the insolvency profession as it relates to receivers.

This information supplements the market information contained in ASIC's first submission.

148 Appointments of receivers, receivers and managers, and controllers account for a relatively small percentage of the total number of annual appointments. For the period July 2008–June 2009, receiver and receiver and manager appointments accounted for 11% and controllers accounted for 6% of all external administration appointments: see Figure A2.1.

Figure A2.1: Total external administration appointments in Australia (July 2008–June 2009)



Note: 83% of the Controller appointments are secured creditor type appointments.

149 During the financial year to June 2009 there were: 152 receiver appointments; 980 controller and managing controller appointments; and 1487 receiver and manager appointments. In total, there were 2619 receiverships.

150 In an economic downturn, such as the recent global financial crisis, secured creditors may be more active in dealing with defaulting loans. This is also reflected in a spike in receivership appointments for companies entering external administration. There was a 105.3% increase in receiverships during the financial year to June 2009 from the previous year (from 606 to 1244). This was following an increase of 35.9% in the financial year to June 2008

(from 446 to 606). Some of this spike is attributable to receivership appointments for some large corporate groups and multiple appointments.

151 Following the usual trend, in the 2009 financial year there was a heavy concentration on receivership appointments in the eastern states of New South Wales (34%), Victoria (27%) and Queensland (24%).

152 While receivers and managers are required to lodge a report with ASIC if an officer contravention is uncovered, only a relatively small number are lodged. Consequently, there is very limited data on receiverships currently available.

153 The majority of receivership appointments are made by banking or financing institutions, which commonly utilise a panel system for the allocation of appointments.

Appendix 3: Related information—Media release

10-90AD 113 Company officers prosecuted in three months

Thursday 29 April 2010

Between 1 January and 31 March 2010, ASIC successfully prosecuted 113 company officers in relation to 212 criminal contraventions of the Corporations Act (the Act).

ASIC took these actions after receiving complaints from the public and insolvency practitioners who have an obligation to report certain offences to ASIC. These prosecutions resulted in fines and costs being imposed totalling approximately $222,200.

Most of the prosecutions relate to company officers failing to comply with their statutory obligations to provide assistance to liquidators and administrators or for failing to provide them with access to a company's books. ASIC also prosecuted directors who failed to update ASIC's public information registers with the current company/officer information and for lodging documents with ASIC knowing they contained false and/or misleading information.

Of the 113 directors prosecuted, 79 were from New South Wales, 15 were from Queensland, 16 were from Victoria and 3 were from South Australia.

The names, offences, results and location of the company officers prosecuted by ASIC is attached in the list below

Background

All 113 directors were prosecuted summarily before the Local and Magistrates' Courts in New South Wales, Queensland and Victoria. All the directors were prosecuted for specific criminal breaches of the Act (see attachment below), with some deterrence activities commencing before January 2010. While the majority of the directors were prosecuted in-house by ASIC lawyers, some of the breaches were also prosecuted by the Commonwealth Director of Public Prosecutions.

Information about ASIC's deterrence activities are contained in individual media releases, available from ASIC's website at **www.asic.gov.au**.

Complaints regarding suspected breaches of the Corporations Act can be lodged with ASIC via our website or by writing to any our capital city offices across Australia:

Misconduct & Breach Reporting
ASIC
GPO Box 9827
IN YOUR CAPITAL CITY

The following attachment is available via hyperlink:

Attachment to 10-90AD 113 Company officers prosecuted in three months

Appendix 4: Related information—Confidential

To assist the Inquiry, ASIC has provided further information in a separate confidential appendix (Appendix 4).

The material in this appendix has been provided to the Inquiry on a confidential basis so as not to prejudice ASIC's ongoing investigations or breach ASIC's legal obligations under s127 of the *Australian Securities and Investments Commission Act 2001* (ASIC Act).