SUPPLEMENTARY SUBMISSION TO SENATE INQUIRY ON LIQUIDATORS AND ADMINISTRATORS

Introduction

Further to the appearance in Adelaide on Friday 9 April of Associate Professor David Brown (with Associate Professor Symes) before the Inquiry, and further to discussion with Richard Grant, I wish to submit further information to the Committee for its assistance in deliberations.

The material below covers two aspects. First, an overview of the regulatory structure of the insolvency profession in the UK. Secondly, information about prohibition orders for persistent non-compliance by insolvency practitioners in New Zealand.

Regulation of the UK Insolvency Profession

The Insolvency Act 1986 (UK) prescribes a regime for the licensing of 'insolvency practitioners' ("IPs") as individuals, which enables them to take on the office of liquidator, provisional liquidator, trustee-in-bankruptcy, administrator, administrative receiver (though these have largely been abolished since 2003), and nominee/supervisor of voluntary arrangements. There are thought to be about 1700 licensed IPs in the UK, a small minority of whom are lawyers, though it is very rare for lawyers to take on appointments.

Insolvency Service

Regulation of the insolvency profession is conducted by the Insolvency Service, an agency of the Department for Business Innovation and Skills (formerly BERR, and before that, DTI). It employs approximately 2150 staff throughout the UK. Its remit includes disqualification of directors, compulsory liquidations and bankruptcies through the Official Receiver.

However, although IPs can be, and are, directly licensed by the Insolvency Service, largely the licensing of IPs is 'delegated' to eight Recognised Professional Bodies. These are:

The Insolvency Practitioners Association, The Institute of Chartered Accountants of England and Wales, The Law Society (England and Wales), The Association of Chartered Certified Accountants. These three bodies cover about 75-80% of the UK profession.

Then there are also The Law Society of Scotland, The Law Society of Northern Ireland, Institute of Chartered Accountants in Ireland, Institute of Chartered Accountants of Scotland.

The Secretary of State has recognised these bodies as having the proper educational, licensing, ethical, complaints and disciplinary procedures in place in order to take on the self-regulatory function. A joint memorandum of understanding exists between the Secretary of State and the RPBs on such matters.

Joint Insolvency Committee

Due to the multiple of self-regulatory bodies involved, it has been necessary for coordination bodies to be put in place. Thus, there is a Joint Insolvency Committee comprised of representatives of the RPBs, and the Secretary of State (R3 and the Northern Ireland Insolvency Service have observer status).

The JIC is the major channel of liaison with the Insolvency Practices Council. The JIC coordinates standard-setting and ethics to ensure consistency among the RPBs in these respects.

All IPs must be qualified by examination as well as experience, and the examination is jointly set and administered by the Joint Insolvency Examining Board. The Insolvency Practitioners Regulations 2005 sets out (reg 6) requirements for 'fit and proper persons', reg 7 sets out appropriate experience and training. There are also bonding requirements for all IPs. In matters such as qualification and ongoing continuing education, the IPs must comply with the requirements of their RPBs. However, the IPA is the only one of the RPBs which is specialist to insolvency.

Monitoring of individual IPs is conducted by each RPB in its accordance with its own procedures. An agreed set of principles for monitoring exists between the government (IS) and the RPBs. Membership, and thus expulsion, from one's RPB, is linked to authorisation to act as an IP. Since 1994 the RPBs have carried out monitoring visits (there had been a Joint Insolvency Monitoring Unit but this was abolished in 2005 so that RPBs now all conduct their own visits). There are differences in the procedures, but the JIC and IPC ensure a broad level of consistency in standards. It is not the case that there are annual visits to IPs by all RPBs, but that option is available under some of their rules. The Insolvency Service also monitors the RPBs, so that it conducts three-yearly monitoring visits of the RPBs themselves.

Insolvency Practices Council

The IPC was formed in 2000 to keep under review the ethical and professional standards of IPs. It can make recommendations to the RPBs and to the Secretary of State. It can take suggestions and concerns from the public and stakeholders, but does not take on individual cases.

R3

R3, the Association of Business Recovery Professionals (formerly the Society of Practitioners of Insolvency), is a professional association which does not have a regulatory/licensing role, but is the major representative, educational and policy-forming association for IPs. It is involved in the development of Statements of Insolvency Practice (see below).

SIPs

Statements of Insolvency Practice are guidance notes issued to IPs on specific aspects of insolvency practice, from time to time as appropriate, commissioned by the JIC, developed by R3, approved by the JIC then adopted by the RPBs. In addition, there is a joint Insolvency Code of Ethics from 2009.

The Codes are binding on members and relevant for disciplinary purposes, and have increasing importance in court decisions when considering standards. Guidance Papers, which are not mandatory, are also issued by the JIC on specific substantive or procedural matters.

Assessment and Reform

The regulation of IPs has been under scrutiny ever since the framework of licensing was established in 1986. In particular, there have been major reviews of IPs' remuneration (the Ferris Report, Working Party on Remuneration of Officeholders, 1998), and the Insolvency Regulation Working Party- Ten Years On (DTI, 1998); IRWP Review of IP Regulation (DTI 1999). Recently the IPC has commissioned research into the complaints handling and disciplinary procedures in the IP profession conducted by Professors Adrian Walters and Mary Seneviratne of Nottingham Trent University, *Complaints Handling in the Insolvency Practitioner Profession*, January 2008. The major finding was that 'complaints procedures are regulatory mechanisms rather than redress mechanism for complaints. They are not seen by the regulators as a substitute for seeking damages or other redress through the courts'. There have also been a number of studies by academics, particularly, Flood and Skordaki's study for the ACCA, *Insolvency Practitioners and Big Corporate Insolvencies* (1995, ACCA).

Despite (or perhaps because of) the plethora of regulatory bodies and agencies set out above, there have still been calls in the UK for a more independent body, particularly to deal with complaints. There have also been calls for a single insolvency regulator, or at least some rationalisation of the number of RPBs. This is something that it is currently being considered by the Office of Fair Trading who are carrying out a market study on corporate insolvency the initial findings of which are expected to be published in June. The idea of an Insolvency Ombudsman was proposed in the Cork Report, but was not taken up by the government when passing the 1986 Act. Subsequent calls have been made by Justice and other groups, for an Ombudsman, as well as for a new oversight body with wider remit than the current IPC, which is confined to general recommendations about standards. A particular concern is independence, since the Insolvency Service can directly license IPs, as well as being the regulator of the other licensing authorities. Nevertheless, since the 1999 Working Party review, which led to the establishment of the IPC, it can be said that there has been no suggestion by the Government that any further oversight body or Ombudsman should be established. The IPC's response to the Walters and Seneviratne report does not suggest that such calls will be heeded in the near future. Given the number of existing agencies and committees involved in the UK, and the Working Party's decision to stick with the self-regulatory or perhaps, co-regulatory, model, it is not surprising that there is no enthusiasm for further bodies to be created in the UK context.

It was reported this week in the UK press (16th April) that the Office of Fair Trading's inquiry into the insolvency profession (which I mentioned to the Senate Committee on 9 April) may recommend (in its first report which is now apparently expected in late June)that the number of Recognised Professional Bodies be drastically reduced.

New Zealand

Whilst New Zealand does not have a system of registration or licensing of its small insolvency profession, it has some control through the disqualifications and disabilities contained in s280 Companies Act. However, there are current Government proposals to tighten up through a 'negative licensing' model, making it easier to remove defaulting IPs.

It seems from the evidence of ASIC that it has no power to (a) either give someone a 'P' plate or (b) to stop them on the road for on the spot infringements. This means that infringements, perhaps other than serious misconduct or criminal activity, will not be sanctioned and dealt with in a timely manner.

In New Zealand a 'prohibition order' may be made (s286 Companies Act 1993) against liquidators, administrators or receivers in case of persistent failure to comply with their duties under any Act, rule of law or rule of court, or direction or order of the court. Applications may be made by various parties. Prohibition orders used to be for up to five years but, since 2006, may be made indefinitely in theory. Evidence of persistent failure is no longer restricted to the previous five years either. Applications may be made by creditors, receivers, the Official Assignee, or directors of a company in liquidation, or shareholders. The court may either order the liquidator to comply, remove the obligation for him to comply, without prejudice to any other remedy.

However, for persistent failures, or serious one-off failures, the court may conclude that the officeholder is unfit to act by reason of the persistent failure to comply. If the court reaches that conclusion, it MUST make a prohibition order, though it has discretion as to the length of the prohibition.

'Persistent failure' may be evidenced, in the absence of good reasons, by two or more occasions on which a court has made an order to comply against the person.

In the case of voluntary administration, provision is made for prohibition orders in New Zealand, even though the provisions are modelled on Australia's Part 5.3A which has no such power in the court.

In the case of liquidation and receivership, the President of the New Zealand Institute of Chartered Acccountants, and the New Zealand Law Society, are respectively given standing to apply.

What this provision (s286 Companies Act 1993) does is provide that any interested applicant, including the relevant professional body, can apply for an order that an IP comply with a duty under statute or law. If at least two such compliance orders are made against the IP, a prohibition order can be made on the basis of persistent failure. While of course the regulator can and should use this provision, it is also available to others, including creditors.

At present, ASIC has the power to bring failures by registered liquidators to adequately perform duties or comply with statutory obligations before CALDB, which can then suspend or cancel registration.

A provision such as section 286 of the NZ statute, in Australia could be recasted to meet the concern of ASIC that it does not have power to issue infringement notices to registered liquidators in respect of one-off or more 'minor' infringements (such as a failure to lodge reports). Arguably, it would be possible for ASIC to be given the power to operate such a system administratively, reserving the involvement of the CALDB to make prohibition orders over a certain period (as with the split jurisdiction of ASIC and the court in relation to director banning orders under the Corporations Act). Query whether one would also want to provide that creditors and others had standing to apply directly to CALDB, or would it be preferable that they apply to court as in New Zealand?

One advantage of the New Zealand provision is that the focus on the number of previous orders for compliance, requiring only two, is an easier test to operate than the 'failed to adequately or properly perform duties' test under s1292 Corporations Act. The tribunal must make a prohibition order, but has a discretion as to the length. This may provide a more powerful deterrent than the practical risk of ASIC taking a case to CALD, or even requiring an enforceable undertaking to be offered. This would be particularly true of a wide range of parties had standing to bring non-compliance before the tribunal, albeit in practice the regulator would be in the best position to identify non-compliance.