



26 January 2011

Ministry of Economic Development
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Insolvency Practitioners Bill – options for regulating insolvency practitioners

The New Zealand Law Society (Society) appreciates the opportunity to participate in further consultation regarding options for regulating insolvency practitioners, as outlined in the paper circulated by the Ministry of Economic Development (Ministry) on 5 January.¹ The comments below supplement the Society's submission on the Insolvency Practitioners Bill.²

Options for Strengthening the Regulation of Insolvency Practitioners

Introduction

The statistics set out under the heading 'Context' in the Ministry paper show that for the 2010 year, 46 percent of liquidation appointments were taken by people who took only one or two appointments and a total of 63 percent had five or fewer appointments in that year.

Any improvement on negative licensing simpliciter is likely to assist in removing the participants who take on one-off assignments. That should immediately benefit the constituency using the services of liquidators, because those individuals who do not typically practise in this area would be discouraged from doing so. That would assist with the issue of competence. It would not necessarily address dishonest and unethical behaviour, nor concerns regarding independence and impartiality. It is nevertheless a good starting point.

Moving to the specific options, it is noted that options C1 and C2 include aspects that are more akin to industry licensing, which could be done as a second phase of work over a three year period. There is some sense in taking a staged approach to this issue because it is important and overseas experience (Australia and England) indicates strongly that how best to regulate insolvency practitioners is a constantly evolving challenge that should not be rushed.

The Society reiterates its view, expressed in its submission on the Insolvency Practitioners Bill, that there is no need for double regulation for any lawyer choosing to practise in this area as lawyers are already regulated under the Lawyers and Conveyancers Act 2006.

¹ *Regulation of Insolvency Practitioners*, Targeted Consultation, 23 December 2010.

² 11 October 2010, available on http://www.lawsociety.org.nz/_data/assets/pdf_file/0017/32921/insolvency-practitioners-bill.pdf.

Option A: Negative licensing with statutory enhancements

Question:

Do you consider that the statutory enhancements outlined [in the Ministry paper], to complement negative licensing, would be adequate to effectively lower the incidence of incompetence, dishonesty and partiality evident in the market at present?

The answer to this question is made in the introductory comment above, that any advance on a pure negative licensing model is likely to deal with at least some of the concerns about competency.

The statutory enhancements would be an improvement on the pure negative licensing model. Nevertheless, the Society does not consider that the enhancements on their own would be adequate to lower the incidence of incompetence, dishonesty and partiality evident in the market at present, because they do not significantly restrict practitioners beyond the existing restrictions. For example, while precluding family members and those with existing personal relationships from taking appointments is a positive measure, anecdotal evidence suggests that these are not significant contributing factors. The insertion of an explicit duty to require independence is no more than is already required in any event and is unlikely to put off those who are dishonest. Equally, the requirement that insolvency practitioners inform creditors of ways and to whom they can complain may not necessarily advance the cause of disgruntled stakeholders. This is because the majority of those who are problem practitioners are unlikely to be members of the New Zealand Institute of Chartered Accountants (NZICA) or of the Society.

That said, the enhanced powers that would be provided to the Registrar of Companies would certainly be a more effective 'after the event' solution, albeit that they do not appear to be a significant advance on the negative licensing model that has been the subject of criticism to date.

In addition, although refinements are not specifically invited, we consider that the following additions would be worthy of consideration were Option A to be preferred:

1. Spot audits of practitioners by the Registrar of Companies.
2. A process for confidential complaints to the Registrar. The reality is that a large number of complaints arise through fellow members of the profession and lawyers in the practice area becoming aware of inadequacies in performance of insolvency practitioners.
3. Finally, the maximum fine for breaching section 280 of the Companies Act 1993 should be increased from \$10,000 to say \$50,000. The Society is aware of one instance in which a receiver had a personal costs award made against him and said as he left court that it was of no concern because he intended to pay himself from the assets in the receivership.

Option B: Option A enhancements and a register of practitioners

Question:

Do you consider that the requirements for registration outlined [in the Ministry paper], to complement the enhanced powers of the Registrar, would be adequate to effectively lower the incidence of incompetence, dishonesty and partiality evident in the market at present?

The establishment of a register of practitioners incorporating a list of banned practitioners would be likely to lower the incidence of incompetence and should go some way towards dealing with dishonesty.

The effectiveness of this register as a tool to counter these problems is dependent upon:

- a) The Registrar being adequately funded and having sufficient competent staff to carry out these functions; and
- b) Educating the business community as to the existence, contents and functions of the register. The incompetent and dishonest prey upon small business owners who are not fully apprised of insolvency processes and who are therefore much easier to mislead.

In relation to funding, an option to consider other than the annual fee or levy on practitioners would be to spread the cost more broadly by, for example, building in the fee or levy to the company's annual return fee, by adding a dollar per return for example.

Option C1: Option A and Option B enhancements with more comprehensive registration requirements (licensing)

Questions:

Is there any requirement missing that would be necessary if the industry moved towards licensing of practitioners? Would it be necessary to establish a disputes resolution process or would appeals to the High Court suffice? Do you consider that licensing is more appropriate and necessary to effectively lower the incidence of incompetence, dishonesty and partiality evident in the market at present? Are the costs of licensing warranted over and above what could be achieved by the first two options (particularly initially)?

There do not appear to be any obvious fundamental requirements missing that would be necessary if the industry moved towards licensing of practitioners. Of note for the Ministry and the Select Committee is that a new code of professional conduct for insolvency practitioners has been implemented and took effect in Australia from 1 January 2011. This is comprehensive and would provide a useful starting point for any code of conduct being considered in this country. This is all the more so given the consideration being given to a Trans-Tasman insolvency convention.

The advantage of a dispute resolution process would be a lower cost for those wishing to dispute a decision by the relevant party or parties as to compliance with the requirements listed. Therefore, whilst it could not be said that such a process was necessary, it would certainly be advantageous for all concerned in order to enable lower cost dispute resolution, thereby leaving only the genuine and significant issues for the High Court.

The Society considers that licensing is more appropriate and necessary to effectively lower the incidence of incompetence, dishonesty and partiality, for reasons that are implicit in the concerns expressed above about options A and B.

Are the costs of licensing warranted over and above what could be achieved by the first two options (particularly initially)? The Society considers that over the longer term, the costs of licensing are warranted if there is to be a genuine attempt to reduce the incidence of incompetence, dishonesty and partiality evident in the market at present. As noted above,

there are various possible ways in which the costs of licensing could be collected and spread over a wider constituency than simply those practitioners who wish to be licensed.

Option C2: Option A and Option B enhancements with co-regulation

Questions:

Is there any requirement missing that would be necessary if the industry moved towards co-regulation of practitioners? Would it be necessary to establish a disputes resolution process that sits outside of the professional bodies? Do you consider that co-regulation will help to lower the incidence of incompetence, dishonesty and partiality evident in the market at present? Are the costs of co-regulation warranted over and above what could be achieved by the first two options (particularly initially)?

This is the option that the Society would prefer to be pursued, whether now or over the next three years.

There is no obvious requirement missing from the co-regulation model set out under option C2.

If it were determined that a dispute resolution process were desirable, then it would be necessary to establish one that sat outside of the professional bodies. This is because neither NZICA nor the Society would have jurisdiction to discipline and deal with disputes with individuals who fell outside their respective constituencies.

The Society does consider that co-regulation would help to lower the incidence of incompetence, dishonesty and partiality evident in the market at present. This is because the co-regulation model proposed would enable the professional bodies and the Registrar to monitor competence and compliance with codes of conduct. In addition, it would be clear to industry participants – including those who are not currently members of NZICA and the Society – that they would be subject to disciplinary processes administered by those bodies.

It is difficult to answer the question whether the costs of co-regulation are warranted over and above what could be achieved by the first two options, since those costs are not currently known. As noted, the number of practitioners who practice in this area during what is currently a significant period of activity for insolvency practitioners is still not very significant. The compliance costs under the Australian model are understood to be in the several thousands of dollars per practitioner per annum. If similar costs were to be imposed on New Zealand practitioners, they would either have to absorb those costs themselves or pass them on through costs charged on particular assignments. Inevitably, increased costs would be easier for larger firms to afford than for smaller firms or sole practitioners. A high cost level per capita may result therefore in competent and honest insolvency practitioners being financially disadvantaged by this model. Plainly, a final view of this could not be expressed until such time as the costs of such a model had been reasonably estimated.

Concluding comments

The comments provided above are brief, having regard to the constrained timeframe and time of year within which comments have been invited. The Society remains willing and interested in engaging with the Ministry and the Select Committee on discussing these options in greater detail.

This submission has been prepared with assistance from the Society's Law Reform Committee and practitioners with expertise in insolvency practice and professional regulation. If you have any queries regarding this submission please contact Vicky Stanbridge, the Committee Secretary, by telephone (04) 463 2912 or email (vicky.stanbridge@lawsociety.org.nz).

Yours sincerely

A handwritten signature in black ink, appearing to read 'Jonathan Temm', written in a cursive style.

Jonathan Temm
President