

New Zealand Law Society

SUBMISSION ON THE INSOLVENCY PRACTITIONERS BILL

Introduction

1. The New Zealand Law Society (the Society) welcomes the opportunity to comment on the Insolvency Practitioners Bill (Bill). The Society endorses the statement in the Explanatory Note to the Bill, that the ability to effectively and efficiently wind up an insolvent company is important in order to protect and promote the integrity of the overall corporate system in New Zealand. The Society agrees that the process of carrying out insolvencies requires practitioners to carry out skilled tasks with sound judgment and integrity.
2. Providing sufficient safeguards to ensure that practitioners have the requisite skills, judgment and integrity should be the touchstone against which the Bill is measured. Insolvency practitioners have a vital role to play and their actions directly impact on the ability of creditors to recover what is owed to them. On the other hand, the Society recognises that there is a cost associated with any regulations. A balance must be struck. In this instance we do not believe the Bill strikes the right balance of achieving workable and effective regulation at a reasonable cost.
3. The Society therefore suggests the following amendments to the Bill:
 - (a) Setting minimum standards for the education, practical training and experience necessary to practice as an insolvency practitioner, including that a practitioner should not be entitled to take appointments in their own name until they have practised under the supervision of another suitably qualified and experienced practitioner for no fewer than three years. The Society would also advocate for an exemption from any minimum standards, on the basis that the regulatory regime governing lawyers under the Lawyers and Conveyancers Act 2006 is more stringent and lawyers should not be double regulated. (This is in line with similar legislation such as the Immigration Advisers Act 2007 (s11)).
 - (b) Extending the application of the Bill to include provisional trustees and trustees appointed to administer Part V proposals under the Insolvency Act 2006.

- (c) Providing a broader definition of related parties than those currently set out in cl 5(1) of the Bill which amends s280(1) of the Companies Act 1993, and cl 13(1) which amends s5(1) of the Receiverships Act 1993.
- (d) Amending cls 5(3) and 13(2) of the Bill, by broadening sub-clause (r) to disqualify not only lawyers struck off the roll of barristers and solicitors, but also lawyers suspended from practising.
- (e) Amending cls 5(3) and 13(2), by ensuring that the proposed new s280(1)(t) of the Companies Act and the proposed new s5(1)(t) of the Receiverships Act are broadened to disqualify not only those with dishonesty convictions, but also those with any conviction that is relevant to the assignment.
- (f) Amending cl 9 of the Bill in relation to the proposed s386N of the Companies Act “Contents of register” to provide that the contents of the register include the details of the insolvencies in respect of which the prohibition order was made.

Negative licensing scheme is necessary, but not sufficient

4. The Bill proposes a negative licensing system that gives the Registrar of Companies (the Registrar) the power to prohibit individuals from providing corporate insolvency services, or to place them under supervision, for up to five years. By its nature, this is an *ex post* system; it is not until some wrongdoing has occurred that the Registrar can step in.
5. For the reasons explained below, the Society believes that the negative licensing model is only one component of a system to improve the quality of those carrying out insolvency assignments, ultimately for the benefit of the stakeholders on whose behalf insolvencies are conducted.
6. The relatively light-handed negative licensing system was developed during the near 10 year economic boom of the late 1990s to 2008. Since that time, the global financial crisis (GFC) has irrevocably changed world financial markets, and the GFC has led to an increase in insolvency work and therefore insolvency practitioners in New Zealand.
7. The growth in insolvency practitioners has raised a concern throughout the economy that a number of these recent entrants may not have a sufficient level of competency to perform their tasks adequately – i.e., do they have the requisite skill, judgment and integrity?

8. The impacts of the GFC have underlined the importance of having the right regulatory structures in place – it is not sufficient to rely on remedies after the event, but rather structures and policies need to be put in place to mitigate risks *in advance*.
9. In this context, it is useful to compare the proposed New Zealand regime in an international context. The jurisdictions with insolvency procedures most similar to New Zealand’s procedures are England and Australia. In both jurisdictions, practitioners must be registered in order to practice. Indeed, in England, the regime is relatively prescriptive:
 - (a) To be registered as an insolvency practitioner, a person must pass three three-hour exams in the core areas of insolvency practice, irrespective of whether they intend to practise in all of them.
 - (b) Applicants are required to show that they are fit and proper to act as an insolvency practitioner, i.e., that they meet acceptable requirements as to education and practical training and experience and that they have in place security for the proper performance of their functions.
 - (c) Registration is renewed on an annual basis.
 - (d) A disciplinary process is also in place.
10. Australia has minimum entry-level statutory criteria for insolvency practitioners, which are administered by the Australian Securities and Investment Commission (ASIC). ASIC also has the responsibility for identifying wrongdoing, with the Companies Auditors and Liquidators Disciplinary Board (CALDB) being the primary disciplinary body.
11. The English and Australian systems are therefore in contrast to the New Zealand system. Both the English and Australian systems require (to varying degrees) that insolvency practitioners have the requisite education, practical training and experience to perform their roles – i.e., some assurance that they can perform their core roles *prior* to their being registered to do so.
12. However, in Australia there is some concern that the system has not gone far enough in terms of regulating insolvency practitioners. A recent report by the Australian Senate’s Economics

References Committee (committee), *The regulation, registration and remuneration of insolvency practitioners in Australia: the case for a new framework, September 2010* (report) contains 17 recommendations for the improvement of the Australian regime.

13. Part II of the report sets out the evidence that regulation of the insolvency industry needs what the committee describes as "significant reform". While much of the evidence referred to is focussed on one corrupt insolvency practitioner, Stuart Karim Ariff, the evidence gathered suggests broader problems that are similar to those experienced in New Zealand.
14. The recommendations include compulsory examinations for applicants and continuing education requirements that must be met before licences can be renewed. The report also recommends compulsory professional indemnity insurance for insolvency practitioners and the establishment of a 'flying squad' with the power to investigate insolvency practitioners.
15. In the New Zealand context, and particularly in the context of this Bill, it is relevant that these recommendations arise out of a more regulated regime, i.e., the Australian regime already has compulsory registration of liquidators and administrators, a regulator and a disciplinary body.

Suggestions for improvements

16. As described above, the Society believes that the object of the Bill should be to ensure, insofar as is possible, that there are sufficient safeguards so that practitioners have the requisite skills, judgment and integrity to perform their tasks. It is acknowledged that there is a cost involved in this. However, the Society believes the suggestions strike the right balance towards achieving workable and effective regulation at a reasonable cost.
17. As drafted, the Bill does not set any minimum standards for the education, practical training or experience necessary to practice as an insolvency practitioner. Such minimum standards are no more than the public might expect of any professional activity. The Bill is deficient in this regard.
18. There are simple and low-cost changes that can be put in place to achieve such objectives.

(a) ***Experience and practical training:***

- (i) Insolvency practitioners should not be entitled to take appointments in their own name until they have practised under the supervision of another suitably qualified and experienced practitioner for no fewer than three years.
- (ii) This mirrors the Society's requirement that a solicitor cannot practise on his or her own account without that supervised period of practice. There are already a sufficient number of qualified and experienced practitioners in New Zealand to supervise aspiring insolvency practitioners.
- (iii) In cases of doubt, the Registrar of Companies could have the ability to confer with the New Zealand Institute of Chartered Accountants (NZICA), the Society and/or INSOL New Zealand, or to review an insolvency practitioner's practice history, to determine whether that practitioner has the necessary qualifications and experience to supervise another practitioner.

(b) ***Educational requirements on registration***

- (i) Minimum educational requirements should also be considered.
- (ii) There is legislative precedent for such requirements. For example, section 15(2) of the Institute of Chartered Accountants of New Zealand Act 1996 provides that one is not entitled to hold oneself out as an 'accountant' unless one is suitably qualified.
- (iii) In order to meet that criterion one must hold "a certificate, degree, diploma, registration, or similar qualification, whether obtained in New Zealand or elsewhere, that is relevant to the practices of accounting and auditing". Section 49 of the Lawyers and Conveyancers Act 2006 is to like effect, albeit with somewhat more stringent requirements.

(c) ***Continuing education***

- (i) In addition to minimum educational requirements to be met, consideration should be given to ongoing continuing education requirements.

- (ii) NZICA, the Society, INSOL New Zealand and various conference organisations regularly present seminars and conferences on insolvency-related topics. Practitioners could be required to provide the Registrar of Companies with an annual certificate that each has undertaken specified continuing education requirements for the relevant period.

19. The Explanatory Note to the Bill highlights concerns that a registration, licensing, or accreditation system would cost several thousand dollars a year per practitioner to operate. Even if that was the case, and the benefits were not considered worthwhile (which the Society questions, given the policy positions taken in Australia), the above minimum standards could be accommodated within the negative licensing regime.
20. Even within that negative licensing framework, the minimum standards should go some considerable way towards improving the quality of service delivered to stakeholders in insolvencies when taken together with the proposed negative licensing scheme described in the Bill.
21. If it is accepted that the negative licensing is not sufficient, and the suggestions above are adopted, then the Society would wish to make further submissions on any minimum standards. Further, the Society would also advocate for an exemption from any minimum standards, on the basis that the regulatory regime governing lawyers under the Lawyers and Conveyancers Act 2006 is more stringent and lawyers should not be double regulated. This is in line with similar legislation such as the Immigration Advisers Act 2007 (s11).

Bill should be extended to cover Trustees under Part V of the Insolvency Act 2006

22. The Society believes that the application of the Bill should be extended to include provisional trustees and trustees appointed to administer Part V proposals under the Insolvency Act 2006.
23. That Act enables individuals who are insolvent but who wish to avoid bankruptcy, to make proposals to creditors to avoid bankruptcy and this may include disposal of property to a trustee for the benefit of creditors. The trustee appointed is not the Official Assignee and there are no qualifying criteria for trustees, although they are subject to statutory duties (ss337 and 338 of the Insolvency Act 2006) once appointed.

Clause 5 - Qualifications of liquidators, and clause 13 - Qualifications of receivers

24. The Society supports the proposed amendments to s280(1) of the Companies Act by the addition of a new subsection (1)(caa) and to s5(1) of the Receiverships Act 1993 by the addition of a new subsection (5)(da). However, it believes a broader definition of related parties than those currently set out in these subsections should be considered.
25. Specifically, parties related to a promoter of a company should be excluded from taking appointments. By way of example, an accounting practice that promotes property schemes should not be entitled to refer the liquidations of unsuccessful participants to the father of one of the principals of the practice. The Society believes that such an appointment would not meet the test of being independent and being seen to be independent, although such an appointment would seem to be allowed under the proposed regime. (Section 245A of the Companies Act 1993 already has a related party definition for disqualifying related party voting that could be applied or amended to suit s280(1)).
26. The Society supports the proposed amendment to s280(1)(cb) of the Companies Act in relation to secured creditors, as drafted (cl 5(2)).
27. The Society supports the additional disqualifying criteria in cls 5(3) and 13(2) of the Bill. Nonetheless, the Society has two comments:
- (a) ***Sub-clause (r) – disqualification of lawyers***
- (i) Sub-clause (r) disqualifies a person who is a lawyer if they have been *struck off*.
- (ii) In contrast, sub-clause (s) disqualifies a person who is an accountant and whose membership of the NZCIA has been revoked or suspended by the NZCIA's Disciplinary Tribunal.
- (iii) The Society submits that sub-clause (r) should be amended to provide that lawyers should also be disqualified if they have been suspended.

(b) *Sub-clause (t) – disqualification for dishonest convictions*

- (i) Sub-clause (t) should be broadened to disqualify from taking appointments not only those with dishonesty convictions, but also those with any conviction that is relevant to the assignment.

28. While the drafting of such a provision may prove challenging, the point is well illustrated by the following example. Mr X was recently appointed as liquidator to a company that owns a multi-storey building that is in need of repairs and maintenance. Not only does Mr X have no experience or training relevant to conducting insolvent liquidations, he also has a recent conviction for undertaking illegal building works. Should creditors (secured and unsecured) have their interests put at risk by allowing control of the major asset of the company to be handed to such a person? As in the case of dishonesty convictions, the conviction for a relevant offence points strongly towards a much higher risk of loss to creditors than would be the case for the appointment of a person without relevant convictions.

Contents of register

29. Clause 9 of the Bill proposes a new s 386N be included in the Companies Act, setting out the required contents of the negative register. The Society believes that the contents of the register should also include the details of the insolvencies in respect of which the prohibition order was made. Creditors of such companies can then be made aware of the offending practitioner's activities. It would also enable those investigating links between offending practitioners and other persons to review past conduct.

Conclusion

30. The Society does not wish to appear in support of this submission. However, if it is accepted that the negative licensing system is not sufficient, and the suggestions in paragraphs 17 – 21 above are adopted, then the Society would wish to make further submissions on any minimum standards.



Jonathan Temm
President
11 October 2010