Review of
Corporate Insolvency Law

Report No. 1 of the Insolvency Working Group, on insolvency practitioner regulation and voluntary liquidations

July 2016

ABOUT THIS REPORT

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About the Insolvency Working Group

The Insolvency Working Group is a panel of experts set up by the government in November 2015 to examine aspects of corporate insolvency law and provide independent advice.

The areas to be looked at are voluntary liquidations including phoenix companies, voidable transactions including Ponzi schemes and regulation of insolvency practitioners. The Insolvency Working Group also has a mandate to examine other areas of potential reform in this area.

This, the first of two reports, covers two of the matters covered in the terms of reference: regulation of insolvency practitioners and voluntary liquidations including phoenix companies. A second report, which will be finalised later in the year, will address the other topics we have been asked to report on, notably voidable transactions including Ponzi schemes and other potential areas of reform.

Members

- Graeme Mitchell (Chair) is a former Deloitte Audit and Assurance Partner. He currently serves as the Chair of the External Reporting Board, and as a Director of CIGNA Life Insurance New Zealand and Barnados New Zealand.
- Michael Arthur is a highly experienced commercial litigator and a Partner at law firm Chapman Tripp.
- Crispin Vinnell is an expert in insolvency and recovery matters and a Partner at law firm Anthony Harper.
- Vivian Fatupaito is a Director at KPMG where she leads the firm's liquidation practice.
- John Fisk is Wellington Managing Partner at PricewaterhouseCoopers with more than 25 years' experience specialising in business recovery services.
- David Young is the Executive Director of Debtworks (NZ) Limited and has extensive debt collection and credit management experience.
- Guy Caro, Senior Solicitor, Ministry of Business, Innovation and Employment, represents the Official Assignee.

Terms of reference

The substantive elements of the terms of reference are attached as **Annex 1**.

Executive summary

This, the first of two Insolvency Working Group reports, addresses the regulation of insolvency practitioners and voluntary liquidations including phoenix companies.

Corporate insolvency arises when a company is unable to pay its debts when they fall due and has liabilities that exceed its assets. The main aim of corporate insolvency law is to provide incentives for any remaining assets of the company to be allocated to their most efficient use. A business should be rehabilitated if it is viable. If not, the company should be liquidated, the assets realised and distributed to creditors in accordance with rules in the Companies Act, and with a minimum of delay and expense.

Insolvency practitioners

Insolvency practitioners (i.e. administrators, deed administrators, receivers and liquidators) play an essential role in achieving those outcomes, and thereby promoting and protecting the integrity of the corporate insolvency system. They must have integrity and skill, and a good understanding of the principles and practices of corporate insolvency law.

Integrity is needed because practitioners are placed in a position of managing and protecting other people's money and property. Consequently, they must act honestly, fairly and impartially at all times, and must avoid any conflicts of interest.

Skill is needed because practitioners' decisions determine whether good outcomes are achieved. For example, judgements exercised by an administrator can impact on whether or not a viable business is rehabilitated. A liquidator's skill can determine whether a company's assets, including claims against wrongdoers, are maximised for the benefit of creditors. Judgements exercised by a receiver or liquidator impact on the total amount that will be available for distribution to creditors.

Unfortunately too many providers of insolvency services fall well short of the standards of integrity and skill that the New Zealand public is entitled to expect. There are self-interested practitioners who overcharge for their services or carry out unnecessary work in order to obtain larger fees. There are 'debtor-friendly' liquidators who fail to comply with their statutory duty to protect the interests of creditors (eg by turning a blind eye when directors have taken assets out of a company prior to liquidation at undervalue or even at no value at all). This problem is particularly evident in relation to small and medium-sized companies.

There are two main causes of the problems.

First, it is too easy for individuals who do not have the required integrity, knowledge, skills and experience to become an insolvency practitioner. Anyone is qualified as long as they are at least 18 years old, are not an undischarged bankrupt, have not been certified under mental health legislation and do not fall within other, narrowly defined, disqualifications.

Second, self-interested and debtor-friendly practitioners are largely unaccountable. They know that they can get away with unprofessional conduct because it is very unlikely that creditors will be able to challenge their actions in the High Court in a cost-effective manner. In addition, it is very difficult to meet the statutory requirements for obtaining a practitioner banning order from the Court. This situation also means that all insolvency practitioners, not just dishonest and grossly incompetent ones, are not sufficiently accountable for negligence under current legal settings.

This situation is unsatisfactory, and we are recommending two main changes.

First, the Insolvency Practitioners Bill (the Bill) that is currently before Parliament includes a number of very useful changes that should be implemented regardless of whether the statutory occupational regulation system also set out in the Bill is introduced. Those changes should be implemented either as is, or with minor modifications. We also recommend some enhancements in addition to those that appear in the Bill.

Taken together, these changes include modifying the list of insolvency practitioner disqualifications, clarifying practitioners' responsibilities, roles and duties, increasing transparency in relation to the appointments of practitioners and improving practitioners' reporting requirements. We are also recommending the removal of legal barriers to obtaining court orders to make orders against unsatisfactory liquidators, by replacing the practitioner on a specific file or banning them from acting as a liquidator.

These changes include narrowing the scope of two liquidator disqualification provisions[1] that are aimed at managing conflicts of interest but in practice capture many situations where no conflict arises. These prohibitions prevent practitioners being appointed in the normal way because (1) they routinely receive insolvency appointments from banks, or (2) they have been appointed as investigating accountants or similar. These provisions cause unnecessary delay and expense because the leave of the High Court is needed to appoint the practitioner.

Second, there is a need for occupational regulation of insolvency practitioners (a licensing system).

The terms of reference asked us to report on the insolvency practitioner registration system contained in the Bill. It proposes that individuals would be required to register if they offer insolvency services. There would be no qualification, experience or good character requirements to become registered. We are opposed to the registration system in the Bill for two reasons. First, it would not contribute to raising standards of professionalism. Second, it has the potential to cause harm because it will mislead inexperienced users of insolvency services into thinking that everyone on the register has been approved by a government regulator as fit to practise.

There is, instead, a need to have a licensing system; i.e. a body with a clear mandate to regulate entry, monitor insolvency practice, and have effective statutory powers to intervene in a timely manner when the need arises. We recommend a professional body/independent regulator co-regulation model. Professional bodies would carry out the frontline regulation. An independent government regulator would monitor and report on the adequacy and effectiveness of the frontline regulator's systems and processes.

We consider that this is the most cost-effective licensing option because it can leverage off the accreditation system regulation that was jointly established this year by Chartered Accountants Australia and New Zealand (CAANZ) and the Restructuring, Insolvency and Turnaround Association of New Zealand (RITANZ).

Voluntary liquidations

The terms of reference also asked us to consider issues around voluntary liquidations. We have included our findings on voluntary liquidations in this report. This is because we consider that much of the harm raised by aspects of the voluntary liquidation process would be reduced by the licensing of insolvency practitioners. In addition, our recommended amendments to the Companies Act 1993 (restrictions on appointments and voiding of certain transfers) and the recommended introduction of Director Identification Numbers would be valuable additions to the existing tools and remedies available to creditors and licensed insolvency practitioners.

[1] Companies Act, s 280(1)(ca)–(cb).

Recommendations

Insolvency Practitioners Bill

R1. Do not proceed with the regime proposed under the Insolvency Practitioners Bill, which allows practitioners to be registered without having adequate qualifications or experience, or meeting a fit and proper person test.

R2. Include other provisions in the Insolvency Practitioners Bill, as is or varied as outlined in paragraphs 84–114, that:

- modify insolvency practitioner disqualifications (paragraphs 86–96);
- clarify and add to the duties, rights and powers of insolvency practitioners (paragraphs 97–106);
- increase transparency in relation to the appointment of insolvency practitioners (paragraphs 107–109); and
- improve insolvency practitioners' reporting requirements (paragraphs 110–114).

Co-regulation

R3. Introduce co-regulation of insolvency practitioners with the following main features:

- a government regulator would:
  - consider applications from professional bodies to be accredited to regulate members who offer insolvency services;
  - set the criteria for accreditation;
  - monitor and report on the adequacy and effectiveness of each accredited professional body's regulatory systems and processes;
  - set minimum requirements to be applied by accredited bodies for licensing insolvency practitioners who provide insolvency services;
  - license overseas-qualified practitioners who are not members of an accredited professional body; and
  - have powers to investigate and prosecute possible contraventions of the law by insolvency practitioners and firms, and individuals who provide insolvency services without holding a licence.
- accredited professional bodies would issue licences to practise and carry out all other aspects of the frontline regulation of insolvency practitioners including:
  - regulating entry;
  - regulating ongoing requirements to retain a licence (eg continuing professional development and adequate insurance cover);
  - promulgating and monitoring compliance with codes of conduct and professional and ethical standards;
  - receiving and investigating complaints and taking disciplinary action where appropriate; and
  - carrying out practice reviews.
- minimum requirements to be met by an individual practitioner would include a fit and proper person test and a test to ensure that the practitioner is sufficiently skilled. Consideration will need to be given to whether some fundamental disqualification criteria should remain in the legislation (eg the age, bankruptcy, mental capacity, disqualification order and crimes of dishonesty disqualifications).
- a register of licensed insolvency practitioners would be established and operated.

R4. Include within the scope of the co-regulation model:

- liquidators (of both solvent and insolvent companies), administrators, deed administrators, and receivers appointed by secured creditors under security instruments in accordance with the

Receiverships Act 1993 (but not receivers appointed under other legislation or by a court); and

- trustees of an insolvent's proposal under the Insolvency Act 2006.

R5. We anticipate that the government regulator may distinguish between solvent and insolvent liquidations. It would be appropriate in our view for that regulator to accredit an organisation to license practitioners who carry out solvent liquidations. Members of an accredited professional accounting body (and possibly the New Zealand Law Society) would, we expect, be sufficiently regulated for that work. That is, provided there was an obligation to immediately transfer the liquidation to a licensed insolvency practitioner if it becomes evident that the company in liquidation is not solvent.

R6. Overseas-qualified practitioners would need to be licensed, or be licensed under an overseas licensing system recognised in New Zealand.

R7. The regime would apply to insolvency practitioners appointed to companies governed by New Zealand statutes (for example New Zealand companies and overseas companies in terms of the Companies Act). Practitioners appointed to other overseas-incorporated entities would not be subject to the licensing system.

R8. Meet the costs of co-regulation in the following ways:

- professional bodies to pay fees to meet the costs of applying to become and continue to be an accredited frontline regulator;
- licensed insolvency practitioners to meet accredited professional bodies costs through fees and levies;
- firms providing insolvency services to pay fees for practice reviews; and
- licensed insolvency practitioners to pay levies to meet all other costs incurred by the independent regulator and to meet the costs of operating the register.

Changes to improve High Court supervision of liquidators

R9. Retain all existing powers under section 284 of the Companies Act relating to High Court supervision of the liquidation of a company.

R10. Make changes that will remove the procedural difficulties associated with the High Court's powers to make orders (a) to enforce a liquidator's duties, (b) to remove the liquidator from office, or (c) to make a prohibition order against a liquidator (by repealing section 286 and transferring those order-making powers to section 284).

Voluntary liquidations

R11. Note that the insolvency practitioner-related changes proposed above will help address the problems associated with voluntary liquidations.

R12. Make the following additional changes:

- prevent company/shareholder appointments of liquidators and voluntary administrators from the date of service of a liquidation application by a creditor, other than with the applicant creditor's consent. A further alternative would be to allow (in addition) the shareholders to apply to court for approval of the nominated liquidator;
- void the transfer of a company's assets once a liquidation application has been filed, other than in the ordinary course of business, where the court has given leave, or where the liquidator has ratified the transfer, save for transfers by an administrator or receiver; and
- introduce a publicly searchable unique identification number for existing and future directors, allocated after a proof of identity process and in addition to existing requirements.

The regulation of insolvency practitioners

Background

1 There are four main types of corporate insolvency processes:[2]

I. **Liquidation** – The liquidation of a company, under Part 16 of the Companies Act, starts with the appointment of a **liquidator**. The liquidator investigates the company's financial affairs, considers why the company failed, reports possible offences, identifies and realises any assets of the company (including claims it may have against directors and others) to pay creditors, pay shareholders (if there are surplus assets remaining after paying creditors in full), then applies to the Registrar of Companies (the Registrar) to remove the company from the register of companies.

II. **Voluntary administration** – Voluntary administration under Part 15A of the Companies Act is a relatively short-term measure (usually about five weeks) that freezes the company's financial position while an **administrator** and the creditors determine the company's future. The administrator reports to creditors on whether the business is viable and can be rehabilitated in whole or in part, or whether the company should be liquidated. The administration period ends at the watershed meeting, where creditors decide whether to adopt a deed of company arrangement, liquidate the company or hand it back to its directors. If a deed of company arrangement is agreed to, it is given effect to by a **deed administrator**.

III. **Receivership** – Receiverships that are governed under the Receiverships Act are usually initiated by a company's secured creditor (usually a bank) based on the terms of the security agreement if the company fails to repay its debts. The **receiver** manages the assets over which the loan was secured in order to repay the debt owed to the secured creditor and amounts owed to preferential creditors. Usually the receiver sells the assets, often by selling the entire business as a going concern. The High Court has an inherent power to appoint receivers, but its purpose is often different to that of a creditor-appointed receivership. In such cases, the Court sets the powers of the receivers.

IV. **Compromises** – An insolvent company can continue operating by agreeing a compromise arrangement with its creditors. A compromise under Part 14 of the Companies Act can be proposed by the board, a receiver, a liquidator or, with the leave of a court, any creditor or shareholder. Part 15 of that Act contains a court-facilitated compromise regime.

2 The Official Assignee is responsible for administering all but a few of the personal insolvency processes provided for under the Insolvency Act. One exception relates to proposals made by an insolvent person to creditors for the payment or satisfaction of his or her debts, under Part 5 of that Act. A trustee gives effect to a proposal that has been approved by a special majority of creditors and confirmed by the High Court.[3]

3 No body corporate may be appointed to any of the offices referred to above. Those offices must be held by natural persons.

[2] Our report focusses on the processes applicable to companies. Liquidation, receivership and voluntary administration are also available to limited partnerships. Incorporated societies and trusts (incorporated or otherwise) may also be liquidated or placed into receivership. We would expect the reforms we propose to apply to all corporate forms, but for convenience, the remainder of our report discusses only the Companies Act regime.

[3] The other exceptions are the supervisor under a summary instalment order, who is appointed by the Official Assignee, and the administrator of an insolvent deceased estate, who is appointed by the court. Because of the means by which each is appointed, we have not considered it necessary to include further reference to those roles in this report.

The status quo – an overview of the market for insolvency practitioners

4 Based on our collective knowledge, along with information from CAANZ, RITANZ, the banking sector and the Inland Revenue Department, we estimate that around 100 practitioners regularly provide insolvency services in New Zealand. Most practitioners are partners or principals in ten or so major accounting firms and firms that specialise in providing recovery, insolvency and turnaround services.

5 The remaining insolvency service providers cannot be readily placed in a single category. Some are specialists who operate in accordance with the independence expectations of corporate insolvency legislation and have the necessary skills and competence. In addition, a small number of insolvencies are carried out by individuals on an *ad hoc* basis. Those individuals tend to have little if any expertise in insolvency law and practice.

Insolvency practitioner regulation in New Zealand

6 Insolvency practitioners are expected to ensure that liquidations, administrations, receiverships and other insolvency processes are carried out efficiently, effectively and with integrity. There is some regulation to support the achievement of these goals. However, there is no legislative occupational regulation of insolvency practitioners in New Zealand. The current system instead comprises the following:

A. statutory duties, and commensurate rights and powers under the Companies Act, Receiverships Act and Insolvency Act;

B. statutory insolvency practitioner disqualifications under the Companies Act and the Receiverships Act;

C. court order-making powers under the Companies Act to supervise a liquidation, enforce a liquidator's duties, or prohibit a person from being a liquidator;

D. the general ethical and professional standards governing those practitioners who are members of professional accounting bodies; and

E. a specialist self-regulation accreditation system operated by CAANZ and RITANZ for their members.

7 Each of these elements is discussed below.

A. Statutory duties, rights and powers

8 The Companies Act, Receiverships Act and Insolvency Act impose duties on liquidators, administrators, receivers and trustees and provide them with powers and rights. These duties, powers and rights are discussed below.

Liquidators

9 Liquidators have a principal duty under the Companies Act to carry out the following activities in a reasonable and efficient manner:

- to take possession of, protect, realise and distribute the assets, or the proceeds of the realisation of assets, of the company to its creditors in accordance with the Act; and
- if there are surplus assets remaining (after paying creditors in full), to distribute them, or the proceeds of the realisation of the assets in accordance with the company's constitution or in

accordance with the Act.[4]

10 Without limiting the principal duty, liquidators have other duties, including:

- listing the people who are owed money, and investigating and reporting on the company's affairs;[5]
- keeping accounts and records of the liquidation;[6]
- having regard to the views of creditors and shareholders, including summoning meetings of creditors or shareholders;[7] and
- reporting suspected offences by the company or any director of the company to the Registrar.[8]

11 Liquidators assume custody and control of the company's assets with effect from the commencement of the liquidation.[9] They are necessarily provided with a broad general power to carry out their functions and duties.[10] In addition, there are 15 specific powers,[11] and other general powers to obtain documents and information,[12] enforce the liability of shareholders and former shareholders[13] and disclaim onerous property.[14]

Administrators and deed administrators

12 Administrators have similarly broad powers, reflecting their need to assume control of the business, property and affairs of the company during the period of the administration,[15] investigate the company's affairs,[16] report to creditors, and call and chair creditors' meetings.[17] Administrators also have responsibilities to report misconduct and other matters to the Registrar.[18] Administrators do not usually determine claims by creditors, realise assets or pay creditors.

13 The powers of a deed administrator, who may or may not be the same person as the administrator,[19] are prescribed by the deed of company arrangement under which he or she is appointed.[20] Deed administrators usually have powers to admit or reject creditors' claims and have a duty to oversee the realisation of assets. They must not do anything inconsistent with the deed of company arrangement, except with the permission of the High Court.[21]

Receivers

14 Receivers have similarly broad powers, rights and obligations in relation to the property in receivership.[22] In addition, receivers have general duties to act in the interests of the person who appointed him or her, and in good faith and for a proper purpose.[23] The purpose of the good faith and proper purpose duties is to ensure that the receiver considers the interests of all creditors, where that

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[4] Companies Act, ss 253 and 313(4).
[5] Companies Act, ss 255(2)(c) and 257.
[6] Companies Act, s 256.
[7] Companies Act, s 258.
[8] Companies Act, s 258A.
[9] Companies Act, s 248(1)(a).
[10] Companies Act, s 260.
[11] Companies Act, Schedule 6.
[12] Companies Act, ss 261–262.
[13] Companies Act, s 268.
[14] Companies Act, s 269.
[15] Companies Act, s 239V.
[16] Companies Act, s 239AE.
[17] Companies Act, s 239AK and subparts 7-8 of Part 15A.
[18] Companies Act, ss 239AH-AI.
[19] Companies Act, s 239B.
[20] Companies Act, ss 239ACO and 239ACS(d).
[21] Companies Act, s 239ACQ.
[22] Receiverships Act, ss 14–15, 19, 21–24, 28 and 40C.
[23] Receiverships Act, s 18.

is not contrary to the interests of the security holder.

Trustees

15 After the High Court approves an insolvent person's proposal, the trustee has duties to take control of the property that is subject to the proposal, administer and distribute that property according to the terms of the proposal and generally give effect to the proposal.[24]

B. Practitioner disqualifications

16 The Companies Act includes a list of items that disqualify a person from being a liquidator unless the Court orders otherwise.[25] These disqualifications can be categorised as follows:

- *inexperience* – a person less than 18 years old;
- *conflicts of interest* – a creditor, shareholder, director, auditor, or receiver of the company, or a person who has had one or more of several specified close relationships with the company in the preceding two years;
- *indicator of financial incompetence or dishonesty* – an undischarged bankrupt;
- *mental incapacity* – a person certified under mental health legislation; and
- *prohibition* – a person prohibited, banned or disqualified from a position of responsibility under the Companies Act, Receiverships Act and some other Acts.

17 The same disqualifications apply to administrators and deed administrators.[26]

18 In addition, a court can make a prohibition order if it is satisfied that the person is unfit to act by reason of persistent failures or a serious failure to comply with a relevant duty as an administrator, deed administrator or liquidator.[27]

19 The disqualifications for receivers are similar to those applying to liquidators, but modified to reflect their different role, particularly in relation to conflicts of interest.[28]

C. Court orders

20 Sections 284 and 286 of the Companies Act include powers for the High Court to make orders under certain circumstances.

Court supervision of liquidation

21 Section 284 of the Companies Act provides powers for various parties to apply to the High Court to intervene in a liquidation. An application can be made by a liquidator, liquidation committee or, with the leave of the court, a creditor, shareholder, other entitled person, or director of the company in liquidation. Among other things, the Court:

- may give directions to the liquidator in relation to any matter arising in connection with the liquidation; and
- may confirm, reverse or modify an act or the decision of the liquidator.

22 The courts will not use this power to overturn decisions made by liquidators reasonably and in good faith. In *Re Optimisationz (in liq); Young & Associates Ltd v Ruscoe*, it was stated that the courts will only interfere if it has been shown that there have been serious and obvious lapses in judgement on the part

[24] Insolvency Act, s 337.
[25] Companies Act, s 280.
[26] Companies Act, ss 239F(2)(a) and 239ACD(2)(a).
[27] Companies Act, s 239ADV.
[28] Receiverships Act, s 5.

of liquidators.[29]

23 Section 284 also empowers the court to order a liquidator to review or fix the liquidator's remuneration at a level which is reasonable in the circumstances, and order the refund of an amount if the total amount retained by the liquidator as remuneration is found to be unreasonable.

Orders to enforce liquidator's duties and prohibit a person from being a liquidator

24 Section 286 of the Companies Act empowers various parties to seek court orders to enforce a liquidator's duties. An application can be made, among others, by a liquidator, a person seeking appointment as a liquidator, a liquidation committee, a creditor, shareholder or director of the company, a receiver and the Official Assignee.

25 The court cannot remove a liquidator from office unless a court has first found that the liquidator had not complied with a duty and made an order requiring compliance. If it is then demonstrated that the liquidator failed to comply with that order, then a court can make an order removing the liquidator from office for the purpose of that liquidation.

26 Section 286 also includes powers for a court to make orders prohibiting a person from being a liquidator for a specified period or an indefinite period if there have been persistent failures to comply, or at least one serious failure to comply.[30] This includes a provision stating that evidence that a court has twice made an order to comply under section 286 in respect of the same person provides evidence of persistent failures to comply, in the absence of special reasons to the contrary (the two strikes rule). For reasons explained later in this report, section 286 is largely ineffective. We recommend a change which would lead to section 286 being repealed and section 284 strengthened.

D. Ethical and professional standards

27 Insolvency practitioners who are also members of professional accounting bodies are subject to ethical and professional standards that apply to all members of the body. The *Code of Ethics for Professional Accountants*[31] issued by the International Ethical Standards Board for Accountants is the foundation for the codes of ethics issued and enforced by the two main professional accounting bodies in New Zealand (CAANZ and CPA Australia). This Code of Ethics is based on the principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

28 CAANZ and CPA Australia both have other ethical and professional standards, including a mandatory insolvency engagement standard.[32]

E. Self-regulation

29 Self-regulation by CAANZ/RITANZ is a new feature of the system for regulating insolvency practitioners in New Zealand. It came into force on 1 January 2016 and has the following main features:

- minimum entry and ongoing qualification requirements, including a requirement to have a CAANZ Certificate of Public Practice (or equivalent for RITANZ-only members), minimum practical experience on entry, a fit and proper person test, ongoing practice review and continuing professional development;
- adequate professional indemnity insurance; and
- a complaints and discipline regime underpinned by a code of ethics and an insolvency

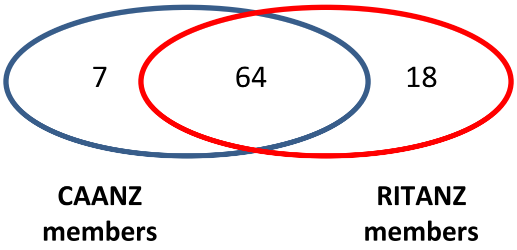
[29] [2012] NZCCLR 23 at [8].
[30] There is an equivalent power for receivers under s 37 of the Receiverships Act.
[31] International Federation of Accountants website, https://www.ifac.org/system/files/publications/files/ifac-code-of-ethics-for.pdf.
[32] Insolvency Engagement Standard *Insolvency Engagements* (NZICA/CAANZ) and Accounting Professional & Ethical Standard - 330 *Insolvency Services* (CPA Australia).

engagement standard.

30 The CAANZ/RITANZ accreditation scheme uses the regulatory systems and structures that the New Zealand Institute of Chartered Accountants (NZICA) is required to have in place to regulate New Zealand resident members of CAANZ in the practice of accountancy in New Zealand with reasonable skill and care under the New Zealand Institute of Chartered Accountants Act 1996.[33] These include a requirement to regulate admission and cessation of membership and requirements to have a Professional Conduct Committee to investigate complaints, a Disciplinary Tribunal to hear complaints referred by the Professional Conduct Committee and an Appeals Council to hear appeals from the Disciplinary Tribunal.

31 There were 89 registrations under the CAANZ/RITANZ accreditation system as at 31 May 2016 (see Figure One) and eight pending applications. Of the 89 accredited practitioners, 51 are based in Auckland, 11 in Christchurch, 11 in Wellington and 16 in other centres.

Figure One: Accredited insolvency practitioners (as at 31 May 2016)



Consideration of practitioner regulation over the last 30 years

32 Insolvency practitioner regulation has been considered four times in the last 30 years:

- as part of the review of company law in the late 1980s and early 1990s that led to the replacement of the Companies Act 1955 with the Companies Act 1993;
- a review of insolvency law in the late 1990s and early 2000s;
- the Insolvency Practitioners Bill, which was introduced into Parliament in 2010 and has not been enacted; and
- CAANZ/RITANZ self-regulation of their members, which was formally proposed in 2013 and, as stated above, came into force on 1 January 2016.

33 Each of these processes is discussed in **Annex 2**.

International norms on insolvency practitioner regulation

34 We consider that the absence of comprehensive occupational regulation means that New Zealand is not within the range of internationally accepted regulatory insolvency practitioner systems for a developed country. The countries that we usually compare ourselves with all have formal insolvency practitioner regulation systems.

35 In Australia there is a requirement to be licensed by the Australian Investments and Securities Commission to be appointed to any type of insolvent external administration (i.e. liquidations, administrations and receiverships). To obtain a licence, the person must:

- have certain base-level qualifications;
- have experience in winding up bodies corporate;
- be capable of performing the duties of a practitioner;

[33] New Zealand Institute of Chartered Accountants Act, s 5A.

- not be a person disqualified from managing corporations;
- be generally resident in Australia;
- have the required performance bond and insurance arrangements; and
- otherwise be a fit and proper person.[34]

36 The licensing system in Australia will be strengthened when the Insolvency Law Reform Act 2016 is brought into force in 2017.

37 How far New Zealand is out-of-step can be illustrated by considering the Cayman Islands Insolvency Practitioner's Regulations 2008. These Regulations stated that in order to be an official liquidator in the Cayman Islands a person must:

a. comply with certain rules relating to residence, independence and professional indemnity insurance; and
b. either:
    i. be qualified as a professional accountant by a relevant institute, be in good standing with such institute, have a minimum of five years' experience in the restructuring or winding-up of businesses, and be credited with not less than 2,500 chargeable hours of work in that area; or
    ii. be licensed as an insolvency practitioner in the United Kingdom, Ireland, Australia, New Zealand or Canada (our emphasis).[35]

38 Two important conclusions can be drawn from the Caymans Regulations. First, they broadly illustrate the type of requirements that are usually included in a system for regulating insolvency practitioners. Second, they indicate that the Caymans Government took it for granted that a country like New Zealand would unquestionably have a robust insolvency practitioner licensing system.

Problems with the status quo

39 The problems with the status quo can be broadly categorised as relating to unprofessional conduct and incompetence. These are not mutually exclusive categories and there is often no clear delineation between them in practice. Four examples are given below.

Example 1: Self-interest

40 The main characteristic of self-interest is where the practitioner charges excessive fees, or carries out unnecessary work in order to generate additional fees. It is not unusual for the fees charged to absorb most or all of the available assets, leaving little if any money for distribution to creditors. This is inconsistent with the principal statutory duty to administer insolvencies in a reasonable and efficient manner, and the requirement to charge reasonable fees. Practitioners who routinely place their self-interest first also tend to have little regard for the other more specific statutory duties.

Example 2: Debtor-friendliness

41 Debtor-friendliness most commonly arises where a liquidator is appointed by the insolvent company's directors or shareholders, acts predominantly or solely in the interests of those who appointed them and fails to protect creditors' interests.

42 An example of debtor-friendly conduct is where claims against the company's shareholders or directors are not pursued in the liquidation. One situation in which this happens is where the assets of a failing company (OldCo) have been transferred by the directors to another company (NewCo) prior to the

[34] ASIC website, http://asic.gov.au/for-finance-professionals/registered-liquidators/.
[35] Appleby eAlert, *Cayman Islands: Overhaul of Insolvency Legislation modernises process, regulates practitioners and promotes cross-border co-operation*, January 2009 http://www.applebyglobal.com/publication-pdf-versions/e-alerts/cayman-islands-overhaul-of-insolvency-legislation-january-2009.pdf.

liquidation at undervalue, or even no value. This type of situation, which is commonly referred to as 'phoenixing', is contrary to insolvency law because fair value should be obtained from the sale of assets. The expectation is that the liquidator will seek to recover assets that were disposed of at undervalue or no value and add them to the pool of assets available for distribution to creditors. However, debtor-friendly practitioners do not do this.

43 A second example of debtor-friendliness is where the debtor has made preferential payments prior to the liquidation of OldCo to one or more creditors. This may include paying amounts owed to themselves, a spouse or partner, a close relative, or another business in which they have a financial interest. Alternatively, it might involve payments to one or more of OldCo's trade creditors in full. The motivation for OldCo's director(s) is to maintain good relations with trade creditors in order to have sources of supply for goods and services to NewCo. However, the expectation in these circumstances is that the liquidator will seek to claw back preferred payments if the expected costs of doing so are less than the amount of the preferred payment. Again, debtor-friendly practitioners do not do this.

Example 3: Substandard decision-making

44 This problem is mostly associated with practitioners having insufficient skills or experience to make high-quality decisions. It is usually more difficult to demonstrate that a practitioner is incompetent because it often comes down to whether or not the practitioner exercised good judgment, based on the particular circumstances. These judgments relate to such matters as whether the practitioner identified the best potential buyers for the company's assets, made sound decisions about whether to sell assets individually or together or obtained satisfactory prices, given market conditions at the time the business or assets of the business were sold.

45 There are also competence issues in relation to individuals who carry out insolvencies on an ad hoc basis, but lack the training and experience to carry them out to the required standard. Although ad hoc appointments are unusual, there can be significant harm to individual creditors in these cases, because they will be out of pocket. It can, in some cases, lead to other companies that are unsecured creditors also failing. Ad hoc appointments can also raise professionalism issues, particularly if the appointee has a conflict of interest due to having close connections to a director of the insolvent company.

Example 4: Sporadic issues

46 As with all professions, there are issues relating to mistakes or errors of judgment that any good practitioner might make. While these lapses may not indicate systemic incompetence or unprofessionalism, the current statutory settings do not always provide for the practitioner to be held sufficiently accountable, due to barriers to creditors seeking redress through the courts.

Specific examples of problems

Gilbert Chapman

47 Professionalism and competence issues were both apparent in *Rai v Chapman*.[36] The court criticised the liquidator (Gilbert Chapman) for delaying a meeting of creditors because he knew that Mr Rai, who was the director and shareholder, wanted him to be replaced:

> It is a matter of good governance that liquidators have to be accountable to creditors. Accountability can be achieved by allowing meetings to be held between creditors and the liquidator. Accountability may be reduced if there is not the machinery available to require meetings and to require a liquidator to appear at the meetings to answer the creditors for the conduct of the liquidation. A simple comparison would be this. Imagine, for example, that the directors of a company put off calling an annual general meeting, knowing that the shareholders would not have them voted back in again and stayed in office by stalling an annual general meeting. That would be reprehensible conduct. Mr

[36] *Rai v Chapman* (unreported), 30 July 2010, Bell AJ, CIV-2010-404-002300.

Chapman's tactic of stalling on calling a creditors' meeting falls into the same category.[37]

48 The court also criticised Chapman for not keeping the company running until the sale of the business had been completed (the company was solvent and had entered into a sale of its business prior to appointing Mr Chapman as liquidator):

> Unless there was anything unusual appearing, there would certainly be no harm in leaving existing management to carry on running the business up until the sale of the business. This was not a receivership. It was not a case where there was any pressing need for an insolvency practitioner to take over running the company himself. Nevertheless, that was the decision that was made… My view is that that decision was a mistake… Accordingly, I see the liquidator as personally responsible for creating a lot of the difficulties that the company got into. A lot of his effort was spent in catch-up in trying to put right the position that the company got into. In particular, there was the problem of the liquidator accepting a reduced price.[38]

Patrick Norris

49 In a criminal case taken by the Police, a liquidator (Patrick Norris) was convicted of theft by a person in a special relationship under the Crimes Act 1961.[39] Norris had been appointed liquidator for Astra Enterprises Limited and instructed his staff to create invoices for $80,960.51. Astra's money was used to buy items and repay debts of Norris Management Services Ltd and Norris. The District Court stated that there was "a blatantly dishonest course of action to try to cover up Norris's failure to deal with or account for the property of Astra to the creditors".[40]

50 Norris was sentenced to home detention, community work and reparation.[41] In dismissing Norris's appeal against his conviction, the Court of Appeal noted the money was not Norris's to use as he liked, but was earmarked for creditors.[42]

The liquidation of Waterloo Buildings Ltd

51 Brent Clode, the sole director of Waterloo Buildings Ltd and two associated companies, appointed three liquidators over a period of less than 12 months in 2008 and 2009. There were independence and other issues in relation to all of these appointments. First Clode appointed his brother-in-law, Michael Cooper.[43] Next he appointed his brother, Peter Clode, a United States resident, to replace Cooper. Clode then sought to appoint a friend, Melissa Watson, to replace his brother. Watson's appointment was challenged by a creditor under section 284 of the Companies Act.[44]

52 Although the judge found there was a factual foundation for the creditor's suspicion that the liquidator did not have the necessary qualifications, experience, independence and impartiality, he considered the applicants had yet to demonstrate an "overwhelming lack of independence on the part of [the liquidator] or great urgency" and was not prepared to complete the review of her appointment without giving Watson a proper opportunity to respond and be heard.

53 In commenting on this case, Russell McVeagh noted that the court will take a cautious approach which may require very persuasive evidence that the liquidator does not meet the requirements of the Companies Act. This standard will be higher again where the liquidator has not had an opportunity to

[37] ib id at [18].
[38] ib id at [6], [28] and [29].
[39] R v Norris (unreported), 16 October 2012, DC CRI-2011-042-1272.
[40] Norris v R [2013] NZCA 526, at [26].
[41] R v Norris (unreported), 24 January 2013, DC CRI-2011-042-1272.
[42] *Norris v R* [2013] NZCA 526 at [32].
[43] Cooper had been bankrupted twice, from 2000-2003 and 2005-2008, Insolvency Register, Insolvency and Trustee Service.
[44] *Fisher International Trustees Ltd and anor v Waterloo Buildings Ltd (in liquidation) and ors* HC AK CIV-2009-404-00640 12 November 2009.

be heard.[45]

54 The High Court appointed the Official Assignee as the liquidator five weeks later.[46]

The causes of the problems

55 The problems arise for three main reasons:

I. the ease of becoming an insolvency practitioner;
II. the difficulty holding practitioners to account for failing to comply with their statutory duties through the court system; and
III. the absence of any requirement for practitioners to operate in accordance with professional and ethical standards.

Cause I: The ease of entry

56 It is too easy to become an insolvency practitioner because the disqualification criteria in the Companies Act and Receiverships Act are minimal. There are no meaningful competence-related criteria. In addition, the criteria relating to honesty and integrity are well short of being comprehensive. The Kamal case, discussed below, is a recent demonstration of the limits of those criteria.

Cause II: The difficulties of holding practitioners to account for failing to comply with their statutory duties

57 It is very difficult to hold practitioners to account for failing to comply with their statutory duties under the current legislative and regulatory settings.

58 Secured creditors have the option of protecting their interests by appointing a receiver. However, decisions to appoint receivers are not taken lightly because of the expense. It is usually not an option for a secured creditor to appoint a receiver unless it has substantial financial exposure.

59 Other creditors rarely have incentives to seek court orders under sections 284 and 286 of the Companies Act to supervise liquidations or to enforce a liquidator's duties. This is particularly so for an unsecured creditor given the substantial costs of taking court action, the uncertainties about whether the action will be successful, and that any gains from a positive outcome will usually be indirect and shared among all unsecured creditors on a pro rata basis.

60 Three cases illustrate different aspects of the difficulties of holding a liquidator accountable under sections 284 and 286.

Case No. 1: The Commissioner of Inland Revenue v Imran Mohammed Kamal

61 In early 2013, Imran Kamal was sentenced to home detention and community service for aiding and abetting false income tax and GST returns and in providing misleading information to the Commissioner of Inland Revenue by way of altered tax invoices. In 2014 Kamal was appointed as liquidator to two companies (known as Hillman and GDZ). He failed to comply with a liquidators' duty to hold a meeting of creditors after receiving valid notices from the Commissioner to do so.[47] In 2016, the Commissioner applied for a 5-year prohibition order against Kamal under section 286. Kamal had resigned as liquidator of the companies before the Commissioner began the proceedings.

62 The High Court held that the Commissioner could not access the section 286 prohibition order

[45] *Russell McVeigh Litigation Update*, March 2010, http://www.russellmcveagh.com/Portals/1/Documents/Litigation%20Alert%20Archive/LitigationMar2010_285html#ReviewandRemoval

[46] Insolvency Detail Report with Asset Progress Updates, Insolvency and Trustee Service, 11 January 2010, https://www.business.govt.nz/companies/app/service/services/documents/AA15F2F5539CBF0491B8DE47905FC8E3

[47] [2016] NZHC 1053 [19 May 2016] at [6]-[11].

jurisdiction solely on the basis of Mr Kamal's convictions under the Tax Administration Act 1994 because there is no fit and proper person test in the list of disqualifications under section 280.[48]

63 The Court also held that once Mr Kamal had resigned he was no longer bound by the liquidators' duties on which the Commissioner relied.[49] Associate Judge Smith concluded the following:

> [77] I acknowledge the Commissioner's concern that the (arguably unfortunate) consequence of the view to which I have come is that a defaulting liquidator will always be able to avoid a prohibition order by the simple expedient of resigning before the creditor's proceeding is commenced.
>
> [78] That may be the case, but the Court's power to impose a prohibition order (at least on the application of a creditor) appears to have been deliberately limited [by Parliament] to those situations where a recalcitrant liquidator has (i) failed to heed the creditor/plaintiff's notice and (ii) remained in office. If that limitation was not in fact intended, I think that is something to be corrected by the legislature; the wording of the statute cannot be stretched to bear a contrary interpretation.

64 In our view, the purpose of the Court's jurisdiction to ban persons from accepting liquidation appointments is to protect the public in relation to future appointments. The fact that the person may have resigned from the particular appointment(s) does not reduce any risk to the public in respect of future appointments.

Case No. 2: The Official Assignee v Norris

65 The Official Assignee applied for a prohibition order under section 286 against Patrick Norris, the practitioner who was convicted under the Crimes Act 1961 (see paragraphs 49–50 above). Proceedings were filed after the Registrar had received complaints about eight separate liquidations that Norris had handled.

66 Although it is clear from a High Court decision in an interlocutory proceeding[50] that several mistakes were made in pleadings, it is also evident that it is very difficult to obtain a prohibition order under section 286. A number of conditions need to be satisfied in a certain sequence over a potentially long period of time before a court can impose a prohibition order. This includes the possibility that the proceedings will be delayed by the practitioner seeking as many adjournments as possible.

67 The proceedings were withdrawn by consent once Norris had been convicted and consequentially became ineligible under current legislative settings to continue acting as a liquidator.

Case No. 3: McMahon v Ah Sam and Vlasic

68 In the McMahon case, there was no suggestion that the liquidators had in any way acted in an inappropriate manner. However, the case did clarify the scope of section 284. Although there have been divergent judicial approaches on this matter, it now appears that there are no powers to remove a liquidator under section 284. In a number of cases the Court has made orders removing a liquidator under section 284 but in those cases the jurisdictional issue was not addressed. It was addressed in *McMahon v Ah Sam and Vlasic*.[51] The Court found that section 284 did not give a wide-ranging power to remove a liquidator and that the Court's removal power was limited to the specific and narrow power under section 286.

69 In *McMahon*, the Court also noted that under the Companies Act 1955 a liquidator could be removed by the Court "on cause shown".[52] The Court also stated the following:

> [34] Section 286 has been criticised as being too narrow. It is when compared with the wide-ranging

[48] ib id at [55]-[58].
[49] ib id at [68]-[70].
[50] HC NEL CIV 2011-442-80 [2012].
[51] [2014] NZHC 659.
[52] op cit, at [10]-[11].

> power under the Companies Act 1955, but the intention was clearly to spare liquidators from being subject to general wide-ranging attacks. They should be removed only if the distinct grounds under s 286 have been made out. That is the policy of the legislation. It is not my job to comment on it further, but simply to apply it.

Conclusions on accountability through the court system

70 Between them, sections 284 and 286 do not provide the High Court with sufficient powers to hold practitioners to account for breaches of their duties for the following reasons:

- the supervisory powers under section 284 do not appear to extend to an ability for the Court to remove a liquidator.
- the Court's ability to remove a liquidator from a particular company under section 286 is limited and onerous.
- an order prohibiting a person from taking appointments over any company cannot be made under section 286 if the liquidator resigned before the applicant began court proceedings.
- the evidential requirements on the plaintiff to obtain a prohibition order under section 286 are very demanding. It is necessary to go to court twice to obtain an order to remove the liquidator, and the whole process can potentially take several months.

71 We recommend changes in paragraph 156 in relation to these matters.

Cause III: The absence of mandatory professional and ethical standards

72 The current Bill focusses on the registration status of the individual practitioner. A process for de-registration of practitioners is created that does not require court oversight. But the step of preventing a person from practising in their chosen field is a very serious one. Judicial review would be possible, so the Registrar, in whom the power is vested, will act cautiously.

73 While a sensible process is needed to remove from the profession those who should not practise, greater confidence in the profession is likely to be generated by a professional disciplinary process that deals with matters that are important, but not serious enough to warrant removal of a person's ability to practise. The absence of any such process from the current statute and the current Bill is a serious limitation.

74 Unsatisfactory practitioners have little incentive to be members of a professional accounting body because it means that they would be subject to formal professional and ethical standards and, therefore, could be at risk of being investigated or disciplined.

75 CAANZ statistics tend to bear this out. Only three out of 156 complaints about New Zealand members related to insolvency practice in the year ended 30 June 2015. Seven out of 84 complaints in the first 8½ months of 2015/16 related to insolvency practice. As at the time of writing, three were still under investigation, two were closed without investigation on the grounds that they were frivolous or vexatious and two were dismissed by the Professional Conduct Committee without adverse finding.

76 Three other complaints that were outside the jurisdiction of CAANZ were made against non-members in the last two years.

Conclusions on the problems

77 The current regulatory regime is unsatisfactory for the following reasons:

- it is too easy for dishonest and incompetent individuals to enter the market.
- almost nothing can be done about practitioner incompetence and dishonesty in individual insolvencies until after the damage has been done.
- it is unusual for anything to be done in practice because it is rarely cost-effective for the parties with standing to seek court orders under sections 284 or 286 to monitor the insolvency

practitioner's performance, or initiate proceedings to challenge dishonest or incompetent practitioners or practitioners who might be negligent.
- the order-making powers under section 286 are, in any case, largely ineffective.

Objectives of insolvency practitioner regulation

78 The main objective is to provide the commercial community with confidence that insolvency processes will be carried out in accordance with the statutory duties. This is essential because insolvency practitioners hold and manage other people's assets in a fiduciary capacity and make decisions that can materially affect the total amount available for distribution to creditors.

79 One aspect of the insolvency practitioner's role is important to bear in mind. He or she works in the interests of creditors, but those creditors are usually diverse and multiple. As a body they have rights and powers, but as individual creditors they have no practical ability to oversee and understand the numerous judgment calls and decisions made by the insolvency practitioner that will affect the economic outcome for creditors.

80 The role of the insolvency practitioner is important for other reasons. Decisions made by administrators and receivers can determine whether insolvent businesses are restructured or liquidated. Thus, the quality of their judgements contributes to determining whether the assets of failed businesses are allocated to their most productive use. Those decisions can also impact on employees and shareholders.

81 There are other secondary objectives:

- assurance that insolvency processes are carried out by honest and competent individuals;
- assurance that insolvency practitioners' firms have the systems and processes needed to support high quality outcomes;
- the importance for New Zealand's reputation that our regulatory systems are consistent with international norms; and
- the need for regulation to be cost-effective.

Options

82 Three sets of decisions need to be made, in the following order:

I. whether to make changes to existing statutory provisions relating to insolvency practitioner disqualifications, duties, rights and powers, reporting to creditors and the means of appointing and replacing insolvency practitioners;
II. whether there is also a need to have an occupational regulation system for insolvency practitioners; then
III. if there is a need for occupational regulation, in which case:
    A. to decide on the range of insolvency processes to which it will apply; and
    B. to consider whether and how the introduction of regulation should affect the role of the High Court.

83 We do not regard the status quo as a viable option, given the serious problems outlined above.

Decision I: Should changes be made to existing statutory provisions?

84 In addition to proposing a registration regime, the Bill proposes numerous other changes to the Companies Act and Receiverships Act. These changes can be grouped into the following categories:

- modifications to insolvency practitioner disqualifications;

- additions and clarifications of practitioners' responsibilities, roles and duties; and
- changes relating to reporting by practitioners.

85 We agree with most of these proposals. We also consider that some further enhancements could be made. We have captured in **Annex 3** to this report a summary of the discussion that follows below, namely:

- the changes currently found in the Bill that we recommend be adopted;
- the (relatively few) changes currently found in the Bill that we do not agree with; and
- the further changes we recommend.

Modifications to insolvency practitioner disqualifications

86 Two of the practitioner disqualification provisions listed in section 280(1) of the Companies Act are too broad. Both of these provisions are targeted at practitioners who have conflicts of interest but, in fact, frequently apply where no conflicts exist in any meaningful sense. These provisions, which are discussed below, cause unnecessary delay and expense because the leave of the High Court is needed to appoint the practitioner. Obtaining these orders, which are generally unopposed and uncontroversial, is an unnecessary expense that is ultimately borne by the creditors. In some cases, the need for that delay and expense mean that appropriate practitioners are not appointed at all. In particular, creditor meetings may vote in favour of another practitioner who does not have the same restrictions.

The continuing business relationship provision

87 Unless the High Court orders otherwise, section 280(1)(cb) of the Companies Act prohibits the appointment of insolvency practitioners as liquidators or administrators where they or their firm have had a continuing business relationship with the insolvent company, its major shareholders or any of its directors or secured creditors within two years immediately before the commencement of liquidation.[53] The problem with this provision is the inclusion of secured creditors and we recommend that it be removed.

88 In New Zealand, most financiers take a general security agreement as security for lending. Because of this, section 280(1)(cb) prevents all insolvency practitioners who have worked for general security agreement financiers (such as the major trading banks) from acting as liquidators or administrators, unless the leave of the High Court is obtained.

89 The existing section does not exclude a practitioner merely because of a banking relationship between the secured creditor and the practitioner or firm, but insolvency practitioners' routine relationships with the major trading banks are often much broader. The more experienced and capable the firm or practitioner, the higher the likelihood that the firm or practitioner will have a 'continuing business relationship' with the trading banks. The existing rule therefore excludes the very practitioners who are the most suitable for appointment. In some cases another practitioner will be appointed simply to avoid the delay and expense.

90 The Bill adopts the approach we recommend.

The professional services relationship provision

91 Another problem arises through section 280(1)(ca) of the Companies Act. Unless the court orders otherwise, this section prohibits the appointment of insolvency practitioners as liquidator or administrator where they (or their firm) have provided professional services to the company within two years immediately before the commencement of the liquidation.

92 Practitioners who have been brought in at the end of the company's trading life and who provide

[53] This section also applies to administrators by operation of section 239F of the Companies Act.

professional advice at that stage are then prevented from acting as the liquidator. The problem is especially acute for investigating accountants who are usually also insolvency practitioners.

93 This situation is problematic for two reasons:

- insolvency practitioners and investigating accountants are selected by, and appointed at the behest of, one of the biggest creditors (a bank) and not the company itself. However, they provide services to the company and so are prevented from acting as liquidators and administrators.
- the existing rule excludes the very practitioners who are the most suitable for appointment (i.e. because they already have a good understanding of the business of the company and are well placed to carry out the insolvency procedure efficiently and effectively).

94 The NZICA Insolvency Engagement Standard may provide a useful approach to follow on this matter. Section 280(1)(ca) is currently more restrictive than this standard. The definition of 'continuing professional relationship' in the Insolvency Engagement Standard excludes situations where the relationship occurs from "the appointment of the member or the firm by, or at the instigation of, a creditor, or other party having an actual or potential financial interest in the entity, to investigate, monitor or advise on the affairs of the entity."

95 The Bill seeks to adopt our recommended approach, but we have serious concerns about the language it uses. Proposed sections 280(2)(d)(i) and 280(3)(a) are not workable in their present form. We recommend language closer to that used in the Insolvency Engagement Standard.[54]

96 We also recommend additions to the list of disqualification criteria under section 280. We believe these amendments will be necessary to ensure conflicted liquidators are not able to accept appointments, which will reduce the risk of harm. Similar provisions should apply to receivers. Our specific proposals are detailed in Table 1, line 1 of Annex 3.

Clarifications of and additions to practitioners' responsibilities, roles and duties

97 We support the following changes in the Bill under this category:

- the requirement for an statement of interests (an 'interests statement'); and
- additional provisions in the event of vacancy of the office of an insolvency practitioner.

98 We also propose reform relating to:

- the insolvency practitioner duty to report serious problems; and
- transparency in relation to appointment of practitioners.

Interests statement

99 Liquidators and administrators will need to file an interests statement in their initial reports and include the updated interests statement in subsequent reports. This amendment will help identify material conflicts of interests for creditors so that informed decisions can be made about the appointment of that insolvency practitioner. The requirements within an interests statement will be prescribed.

Vacancies in the office of an insolvency practitioner

100 In event of the office of an insolvency practitioner being vacant, the Bill adds a new provision for the transfer of documents and control over property (or assistance for receivers) to a replacement insolvency practitioner and creates an offence for not doing so. The provision also applies if a person was acting as administrator before the appointment of a liquidator to a company in administration.

101 The changes will ensure that in the event of replacement insolvency practitioner being appointed there

[54] See the definition of 'continuing professional relationship' in paragraph 9 of Insolvency Engagement Standard.

is an efficient transition process and the replacement has all the documents and control necessary to perform their functions.

Duties to report serious problems

102 A liquidator who considers that an offence that is material to the liquidation has been committed by the company or any director against the Companies Act 1993, Crimes Act 1961, Financial Markets Conduct Act 2013, Takeovers Act 1993 or Insurance (Prudential Supervision) Act 2010 must report that fact to the Registrar.[55] Such disclosures are protected by absolute privilege. The Registrar may supply the report to the Financial Markets Authority if it relates to a financial markets participant.[56]

103 Receivers are subject to similar duties to liquidators and face the same test as liquidators, i.e. disclosure of offences that are material to the receivership, and these disclosures have the same protection.[57]

104 Administrators are also subject to similar duties but must also consider whether any offences have been committed in relation to the company.[58] However, such disclosures in relation to administrations are not currently protected by absolute privilege.

105 The current 'whistleblowing regime' poses numerous problems. First, it is of no importance whether the possible offence is material to the liquidation or the receivership. That test should be removed. Second, the list of statutes is incomplete. Other serious dishonesty-related offences, such as money laundering and tax evasion, should also be reported. Third, the list of agencies that could receive the reports should be further expanded to include the Police, the Serious Fraud Office and the agency responsible for administering the particular Act (if relevant). Fourth, administrators are currently not protected by absolute privilege which may discourage the reporting of suspected offences.

106 Our specific proposals are detailed in Table 2, line 22 of Annex 3.

Increased transparency in relation to the appointment of practitioners

107 The current regime does not require liquidators to notify creditors or the Registrar as to whether the appointment was initiated by special resolution of voting shareholders, the board of the company or by the court through an application, and if so the identity of the applicant creditor. Administratively, the Registrar's online system requires the liquidator to notify whether the appointment was by the shareholders or by the High Court, but there is no statutory requirement to do so, and the identity of the applicant creditor is not disclosed. It would be useful for creditors to know who initiated appointments. This would provide them with information to help determine whether an application should be made to the Court to have the liquidator replaced.

108 The same should also apply to administrators and receivers.

109 Our specific proposals are detailed in Table 2, line 23 of Annex 3.

Improvements to insolvency practitioners' reporting requirements

110 The Bill includes new and more prescriptive reporting requirements for receivers and liquidators. An important improvement is the introduction of a requirement to report cumulative fees and expenses of the liquidator and cumulative amounts received and paid (in summary form).

111 The development of the reporting requirements in the Bill is based on the more detailed requirements already set out in the Receiverships Act. There are currently only very broad requirements in the Companies Act for liquidators. The new provisions for receivers re-state the existing requirements and add further financial information requirements.

[55] Companies Act, s 258A.
[56] Companies Act, s 258B.
[57] Receiverships Act, s 28.
[58] Companies Act, s 239AI.

112 However, we consider that the proposed changes to reporting requirements should go further. There are significant information asymmetries between insolvency practitioners and creditors.

113 Another improvement not yet found in the Bill would be to require liquidators, on completion of a liquidation, to set out in summary form:

- the extent to which unsecured creditors in each class (preferential and ordinary) were paid. That could be a simple and fairly standardised requirement which revealed for example that preferential creditors were paid in full and ordinary unsecured creditors received [x] cents in the dollar; and
- whether there were any recoveries from creditors, directors or shareholders.

114 Requirements of this nature would enable data about the effectiveness of the liquidation process to be more available to consumers of insolvency services. It would not be onerous as liquidators will necessarily have precise details of such matters. For example, it is not possible to pay creditors without establishing the exact percentage that they can be paid. Improvements could also be made to receivers reporting requirements. Our specific proposals are detailed in Table 3, lines 27–29 of Annex 3.

Conclusions on changes to existing statutory provisions

115 Taken together, there are a significant number of changes to the Companies Act and Receiverships Act in the Bill that will materially improve the corporate insolvency system. Those changes should be implemented regardless of whether the statutory occupational regulation system also set out in the Bill is also introduced. Most of those changes can be retained as currently drafted, but a small number could be improved by making minor modifications for workability and practicality.

Decision II: Is occupational regulation needed?

116 We have identified four occupational regulation options.

Option A: Registration as proposed in the Insolvency Practitioners Bill

117 Under this option there are no restrictions on entry apart from the disqualifications in the Companies Act and Receiverships Act, and a requirement to be registered. Registration does not convey any suggestion of honesty, competence or quality of service.

Option B: No statutory occupational regulation

118 Under this option, the statutory occupational regulation system set out in the Bill would not be implemented but the current voluntary CAANZ/RITANZ accreditation system would remain.

Option C: Co-regulation

119 This option would require a licence for a person to practise as an insolvency practitioner.

120 A government regulator would:

- consider applications from professional bodies to be accredited to regulate members who offer insolvency services;
- set the criteria for accreditation;
- monitor and report on the adequacy and effectiveness of each accredited professional body's regulatory systems and processes;
- set minimum requirements to be applied by accredited bodies for licensing insolvency practitioners who provide insolvency services;
- license overseas-qualified practitioners who are not members of an accredited professional body; and
- have powers to investigate and prosecute possible contraventions of the law by insolvency

practitioners and firms, and individuals who provide insolvency services without holding a licence.

121 Accredited professional bodies will issue licences to practise and carry out all other aspects of the frontline regulation of insolvency practitioners including:

- regulating entry;
- regulating ongoing requirements to retain a licence (eg continuing professional development and adequate insurance cover);
- promulgating and monitoring compliance with codes of conduct and professional and ethical standards;
- receiving and investigating complaints and taking disciplinary action where appropriate; and
- carrying out practice reviews.

122 The minimum requirements to be met by an individual practitioner would include a fit and proper person test and a test to ensure that the practitioner is sufficiently skilled. Consideration will need to be given to whether some fundamental disqualification criteria should remain in the legislation (eg the age, bankruptcy, mental capacity, disqualification order and crimes of dishonesty disqualifications).

123 A register of licensed insolvency practitioners would be established and operated.

Option D: Government licensing

124 This option would require a licence for a person to practise as an insolvency practitioner.

125 All licensing functions, as discussed under Option C, would be carried out by a single regulator that is independent of the interests of the profession.

The CAANZ/RITANZ system under each option

126 We expect that the CAANZ/RITANZ accreditation system:

- would be retained under options A and B;
- would form the basis for co-regulation under Option C after being modified to fully reflect public policy objectives, and the requirements imposed by the legislation and the regulators; and
- would no longer be required under Option D.

Analysis of the Options

Option A: Registration as proposed in the Insolvency Practitioners Bill

127 In our view, the registration regime proposed under the Bill is flawed for two reasons:

a. it will not stop unsatisfactory practitioners from entering and participating in the market. The registration system does not address several important entry-related matters, notably qualifications, experience and good character. The principal duty for liquidators in the Companies Act states that the practitioner must carry out the work in a reasonable and efficient manner. There is much too large a gap between that expectation and the grounds for deregistration under the Bill, which is criminality. In practice, the Registrar will not be able to deregister a practitioner for most forms of unprofessional conduct; and

b. the registration regime has the potential to do more harm than good because it will almost certainly mislead inexperienced users of insolvency practitioner services. Company shareholders, directors and creditors who are not regular users of insolvency services cannot be expected to understand the difference between ‘registration’ and ‘licensing’ when those terms are used in their technical senses. On the contrary, we consider it reasonable for the public to expect that if a person's name appears on a government register, then an independent regulator will have first verified that he or she has met certain minimum standards of competence and honesty.

128 For these reasons, we agree with the statement in a consultation document issued by NZICA and INSOL New Zealand in 2013 that the Bill "does not provide any assurance that an insolvency practitioner is competent to practise or is necessarily a fit and proper person".[59] Consequently it will not provide an effective means of protecting creditors from self-interested, debtor-friendly and incompetent practitioners, and nor will it adequately protect the integrity of the corporate insolvency system.

Option B: No statutory occupational regulation

129 Option B has the same problem noted in relation to Option A; there is too large a gap between the standard of professionalism expected under the principal duty and the grounds for disqualification. However, option B is better than option A because it will not provide false comfort to inexperienced users of insolvency services about individuals' competence and honesty.

130 In addition, the current voluntary CAANZ/RITANZ accreditation system will remain for Option B. We are very supportive of the intent of the scheme. This scheme contains all the elements that we consider are necessary to ensure that insolvency processes are carried out by honest and competent individuals. Most importantly, the scheme is underpinned by a code of conduct and the systems and processes to drive compliance by practitioners. We consider that over time, the 'brand' of the scheme will grow and be recognised as a baseline of 'best practice'. This should eventually inform change in the market of who an insolvency practitioner of choice is and provide useful information to the courts.

131 However, this scheme only applies to members of CAANZ or RITANZ or persons who undertake to subscribe to the parameters of the scheme. The scheme has an unavoidable lack of comprehensiveness. We consider that only a modest magnitude of change can be effected by voluntary schemes and only after a significant time lag. This means that, for the foreseeable future, the status quo prevails. We have already outlined why we do not regard the status quo as a viable option.

Option C: Co-regulation

132 Co-regulation would provide three main benefits.

a. it would make it difficult for dishonest and incompetent persons to become insolvency practitioners;

b. it would provide accredited professional bodies with the powers they need to suspend or cancel licences of practitioners who fail to comply with their statutory duties or who misuse their statutory rights and powers; and

c. it would provide for supervision of conduct in accordance with the public's expectations in relation to all accountants in public practice. This would include monitoring compliance with legislative obligations and the accredited body's code of ethics, professional standards (including the insolvency engagement standard) and rules. It would provide for supervision of the range of conduct that membership of a professional accounting body typically entails, such as considering fee disputes and complaints about errors of judgement (eg on conflict of interest matters), or complaints of mistakes or negligence (eg unnecessary delays, or not completing due diligence in relation to the sale of assets).

133 In addition to providing powers to suspend or cancel a licence and/or a certificate of public practice, there would also be powers to reprimand a member, require the member to complete a professional

[59] *Insolvency Practitioner Regulation*, http://www.ritanz.org.nz/wp-content/uploads/Insolvency-Regulation-Consultation-Document.pdf.

development course, impose a monetary penalty, order the investigation of the member's practice, order that the whole or part of a fee be waived or returned and order the member to not undertake specified assignments.

134 These benefits are intangible and we have not attempted to quantify them. However, we give significant weight to them because there is scope for substantial improvement to the effectiveness and integrity of the corporate insolvency system, particularly in relation to liquidators appointed by company directors or shareholders.

135 We do not see a risk of competent individuals being excluded under co-regulation. For example, a qualification regime similar to the current rules of RITANZ should apply. It would be sufficient under those rules if the individual demonstrates sufficient hours of recent experience, insolvency-related experience generally and a proven record of being a fit and proper person.

136 We note that a statutory occupational regulation system for insolvency practitioners would have to comply with the Trans-Tasman Mutual Recognition Act 1997 and other international obligations in relation to overseas-qualified insolvency practitioners. Introducing a statutory co-regulation licensing model would create opportunities for New Zealand practitioners to register and practise as insolvency practitioners in Australia (pursuant to the Trans-Tasman Mutual Recognition Arrangement). It is unclear how much trans-Tasman competition there is likely to be in practice.

Meeting the costs of co-regulation

137 Where appropriate, non-government recipients of specific government activities should usually be charged some or all of the costs of those activities. It is usually inappropriate to recover the costs of such activities as general policy development and law enforcement. However, it is usually appropriate for costs to be recovered in relation to regulatory activities.[60]

138 There are two types of cost recovery charges:

a. Cost recovery fees – fees charged when an activity is provided directly to a specific individual or organisation; and
b. Cost recovery levies – charges imposed when an activity is provided to a group of individuals or organisations rather than to a specific individual or organisation. [61]

139 Applying these definitions, the costs of regulating insolvency practitioners should be met in the following ways:

- professional bodies should pay fees to meet the reasonable costs of applying to become and continue to be an accredited frontline regulator;
- accredited professional bodies should meet all of their costs through fees and levies on licensed insolvency practitioners;
- firms providing insolvency services should pay fees for practice reviews and inspections;
- the Crown should meet the costs of court enforcement by the government regulator;
- licensed insolvency practitioners should pay levies to meet all other costs incurred by the government regulator, including the costs of:
  - operating and maintaining the register of licensed practitioners;
  - developing and maintaining rules, guidelines and other regulatory standards;
  - investigations; and
  - reporting on the performance of accredited professional bodies, licensed insolvency practitioners and firms that include one or more licensed insolvency practitioners.

[60] Australian Department of Finance, *Australian Government Cost Recovery Guidelines*, Resource Management Guide No. 304, July 2014, 3rd edition, paragraphs 10-14.
[61] ib id, paragraph 4.

Option D: Government licensing

140 A licensing regime operated by a regulator would have most of the benefits of co-regulation. In particular, we would expect that government licensing will be similarly effective in protecting creditors from unprofessional conduct and incompetence. However, there are potential differences. A government agency may not achieve the same quality of outcomes as a result of not having as good an understanding of the market as a professional body. On the other hand, an industry regulator may be seen as unduly partial to the interests of its members.

Conclusions on occupational regulation

141 Option A (registration) and Option B (no occupational regulation) are unsatisfactory because they do not effectively deal with the problems identified earlier in this report. This is mainly because of the substantial gap between the grounds for disqualification (eg criminality) and the much higher professional and ethical standards that the public is entitled to expect in relation to individuals who have a statutory responsibility to manage, protect, realise and distribute assets. As the Court of Appeal said in the Norris case, those assets are not for insolvency practitioners to use as they like.

142 We consider that Option C (co-regulation) and Option D (government licensing) are the best two options because they are likely to be equally effective in promoting confidence in the commercial community, which is the main objective. We prefer Option C because it will be considerably more cost-effective, both in terms of one-off and ongoing costs.

143 The only one-off cost under Option C is to establish independent oversight and set up the requirements and processes for accrediting professional bodies. By contrast, Option D will require the establishment of a full regulatory system. There will also be the cost of dismantling CAANZ/RITANZ accreditation, although those costs are likely to be relatively small.

144 Option C is broadly similar to the regime that applies in the United Kingdom under the Insolvency Act 1986 (UK). Under the UK Act, the Secretary of State may declare a body to be a "recognised professional body" if it regulates the practice of a profession and maintains and enforces rules for securing that the relevant members:

- are fit and proper persons to act as an insolvency practitioner; and
- meet acceptable requirements as to education, practical training and experience.[62]

145 Those bodies are charged with 'authorising' persons to act as insolvency practitioners. They may withdraw an authorisation. Decisions to not grant an authorisation, or to withdraw one, can be reviewed by a tribunal. It is an offence to take an insolvency appointment without being qualified to do so.

146 Before detailed work is carried out to design a co-regulation model we consider that a comparison with the UK regime could be undertaken.

Decision IIIA: Processes that should be covered by occupational regulation

147 We consider that it is essential for the licensing system to apply to the full range of processes where the practitioner has duties to manage, protect, realise or distribute other people's assets, i.e., company liquidations, administrations and receiverships, along with trustees under the Insolvency Act. The marginal costs of including all practitioners are very small because there is only one profession in a real sense.

148 For the reasons outlined below, we also consider that:

[62] Insolvency Act 1986 (UK), s 391.

- Solvent liquidations should not be reserved to licensed insolvency practitioners. They should also be able to be carried out by qualified accountants who are members of accredited professional accounting bodies, and possibly law practitioners. Practically, under our model, we would see the government regulator accrediting a wider group of organisations in respect of insolvent liquidations (eg CAANZ and RITANZ in their own right); and

- Compromises should not be included.

Solvent liquidations

149 Solvent liquidations are different from insolvent liquidations for two main reasons:

a. Solvent liquidations can usually be carried out to the required standard by a wider range of persons than insolvency specialists. They do not usually raise complex issues because companies are often put into liquidation in this way simply because a business has been sold, closed down, or reorganised for tax and/or management purposes.
b. The directors must first make and file resolutions as to solvency and the shareholders must then pass a resolution to appoint a liquidator before the liquidation can commence. Thus, there are no creditors' interests to be protected as long as the judgements the directors made at the outset as to solvency subsequently prove to be correct.

150 For these reasons there is no need to reserve solvent liquidations to licensed insolvency practitioners. However, if the person carrying out the liquidation (Person A) is not a licensed insolvency practitioner and becomes aware that the liquidation is not solvent then Person A should be required to immediately transfer it to a licensed insolvency practitioner for completion. We consider that the transfer system will only be effective if Person A is subject to ethical and professional standards, such as those applying to accountants or lawyers. This will ensure that investigation and disciplinary processes can be used if Person A fails to carry out the transfer.

Compromises

151 Under Part 14 of the Companies Act, a compromise arises when a company and its creditors reach an agreement cancelling all or part of the company's debts, varying the rights of its creditors or the terms of the debt, or altering the company's constitution in ways that affect the likelihood of the company being able to pay a debt. Similar outcomes can be achieved through the court-supervised Part 15 process.

152 Although recovery, insolvency and turnaround specialists often advise parties to a proposed compromise, Part 14 does not prescribe an office or role of 'compromise trustee' or set out any specific duties, rights or powers of that person. There is no equivalent to the 'trustee' or 'provisional trustee' described in Part 5 of the Insolvency Act in either Part 14 or Part 15 of the Companies Act. However, Part 14 does include references to liquidators and receivers because many compromises are proposed in connection with companies to which liquidators or receivers have been appointed. The licensing regime would apply to those practitioners in their statutory roles as liquidators and receivers.

153 Persons who manage compromises do sometimes handle other people's money. However, we do not support regulating them. The main benefit of the compromise system is to provide a simple and flexible alternative to other statutory insolvency processes.[63] In order to apply the licensing system to compromises, it would be necessary to create 'compromise trustee' as a statutory office. As with other classes of insolvency practitioners, it would be necessary to define the role and add duties, rights and powers. There is a significant risk that the simplicity and flexibility benefits would consequentially be lost and discourage people from using Part 14.

[63] The compromise system takes up just four pages of the Companies Act. Voluntary administration is 58 pages and liquidation is 66 pages.

Decision IIIB: The role of the High Court

154 In a case considered under section 284 of the Companies Act, the High Court noted that the Act:

> …[puts] all liquidators on an equal footing. That means that the Court's ability to exercise its inherent jurisdiction to supervise liquidators, previously restricted to those appointed by the Court, now applies to all, however appointed…. The fundamental point is that Parliament intended that this Court exercise a general supervisory and, in appropriate cases, involving urgency, summary jurisdiction over them, in a manner akin to the Court's supervision of one of its "officers".[64]

155 Having concluded that a licensing system is needed, a consequential question is what role, if any, the High Court should have. In answering this question, we wish to emphasise that licensing liquidators and the oversight of liquidations are distinct activities. The former is a role for regulators; the latter for the courts. We consider that it is essential for insolvency practitioners to continue to have duties to the High Court, and therefore for the Court to retain its general supervisory role. This approach is consistent with UK legislation.[65]

156 A consequential issue is how to deal with the problems with the removal and prohibition order-making powers under section 286, as summarised in paragraph 70 above, to make them effective. We consider that the Court should be able to make a prohibition order against a liquidator for one bad action (eg theft). We consider that this can be achieved by making the following changes:

- Repeal section 286 (and the related section 285).
- Amend section 284 to include powers to make orders to enforce a liquidator's duties and to provide for removal and prohibition orders.

Conclusions on the regulation of insolvency practitioners

157 Insolvency practitioners hold and manage other people's assets in a fiduciary capacity and make decisions that can materially affect the total amount available for distribution to creditors. Hence, it is essential for the system regulating insolvency processes to provide strong incentives on all practitioners to understand their statutory duties and consistently apply them.

158 The current statutory system does not provide those incentives. It falls significantly short when questions about competence, honesty, ethics, professionalism and accountability arise. While the majority of practitioners consistently manage and administer insolvencies in accordance with the high standards expected of members of any profession, a significant minority take advantage of weaknesses in the system to act in their self-interest, ignore their statutory duties, harm the interests of creditors and damage the integrity of the corporate insolvency system. There is also a general lack of accountability in relation to practitioners who make mistakes or errors of judgment but are not subject to any ethical or professional standards.

159 These outcomes can be attributed to a number of problems with the existing statutory settings. There are two particularly significant deficiencies:

a. It is too easy to enter into insolvency practice, most notably due to the absence of qualification and experience requirements and a fit and proper test.
b. It is rare for any adverse consequences to arise when standards of professionalism are not met. Although there are powers for the courts to supervise liquidations or make orders to enforce liquidator's duties, these provisions are largely ineffective.

[64] *ANZ National Bank Ltd v Sheahan and Lock* HC AK CIV 2011-404-7665 [15 November 2012] at [137].
[65] Insolvency Act 1986 (UK): see section 108(2) "The court may, on cause shown, remove a liquidator and appoint another", and section 112 "The liquidator or any contributory or creditor may apply to the court to determine any question arising in the winding up of a company…"

160 We considered the option of only recommending strengthening the existing statutory provisions to provide for more effective court orders to be made. Although we have recommended improvements of this nature, we consider that these changes alone are not sufficient. Ongoing supervision is required. This is squarely a function for a regulator, not a court.

161 Regulation and litigation tend to differ in four key ways:[66]

- Regulation tends to use preventive means of control. Litigation tends to use deterrent means.
- Regulation tends to use rules. Litigation tends to use standards.
- Regulation tends to use experts to design and implement rules. Litigation is dominated by generalists, although experts provide input as witnesses.
- Regulation tends to use public enforcement mechanisms. Litigation more commonly provides private enforcement mechanisms.

162 All these trade-offs favour regulation, not litigation.

163 We have considered two models of regulation: regulation by an independent government regulator, or regulation by one or more professional bodies overseen by an independent government regulator (i.e. co-regulation). We are recommending co-regulation mainly because much of the 'regulatory infrastructure' already exists. It should be relatively easy to modify CAANZ/RITANZ accreditation to become a frontline regulation system.

164 We have not made recommendations about the responsibility for independent oversight, although the two main options are the Financial Markets Authority or the Registrar. The main argument in favour of the Financial Markets Authority is that it already has several occupational regulation-related responsibilities, including co-regulation through its oversight responsibilities under the Auditor Regulation Act 2011. On the other hand, the Registrar has the relevant sector knowledge due to having both Companies Act enforcement and insolvency-related responsibilities.

165 This is a finely balanced call. The Financial Markets Authority would need to upskill on sector knowledge, while the Registrar would need to upskill on occupational regulation and co-regulation principles and practices. We recommend that the Government consults with both parties before deciding which regulator to use.

[66] Richard A Posner, *Regulation (Agencies) versus Litigation (Courts): An Analytical Framework*, in "Regulation vs Litigation: Perspectives from Economics and Law", ed. Daniel P Kessler, University of Chicago Press, December 2010, p13.

Voluntary liquidations

167 The terms of reference also asked us to consider issues around voluntary liquidations. We have included our findings on voluntary liquidations in this report because we consider that many of the adverse consequences raised by aspects of the voluntary liquidation process would be reduced by the licensing of insolvency practitioners. Regardless of whether licensing is introduced, we also recommend three additions to the existing tools and remedies already available:

a. Prevent company/shareholder appointments of liquidators and voluntary administrators from the date of service of a liquidation application by a creditor, other than with the applicant creditor's consent.
b. Void the transfer of a company's assets once a liquidation application has been served, other than in the ordinary course of business, where the liquidator has ratified the transfer, or where the court has given leave, save for transfers by an administrator or receiver.
c. Introduce a publicly searchable unique identification number for existing and future directors, allocated after a proof of identity process and in addition to existing requirements.

168 A voluntary liquidation is a non-court-ordered appointment of a liquidator to wind up a company's affairs. This is most likely to be initiated by shareholder(s) passing a special resolution (usually 75 per cent of shareholders are required to agree). The creditors of the company are not required to be involved in that decision. The company may be solvent or insolvent at the time the liquidation is commenced.

169 We are mindful at the outset that insolvency law aims to facilitate effective decision making from directors and interested parties about whether to rehabilitate or liquidate a company and that it is important that the voluntary liquidation process is available.

170 The concern about voluntary liquidations is that the process can be misused, in particular the appointment of a debtor-friendly or incompetent or dishonest liquidator who does not pursue claims or other courses of action. For example directors 'phoenix' to a new company free of the liabilities of the old company but with the assets, often transferred at undervalue or at no value, to the detriment of the creditors of the old company.

171 We are also mindful that taking risks in pursuit of benefits means that companies can and do fail. It is the role of insolvency law to provide procedures for efficiently realising and distributing the assets of an insolvent company. This is crucial to the functioning of credit markets and the reallocation of capital. This essential purpose of insolvency law often means that parties are unhappy with the outcome. Whether debtors or creditors are unhappy depends on the particular situation, but there are usually no 'winners'. However, there is no amendment to the law that would guarantee that creditors would never lose money.

Existing provisions

Valid and invalid concerns about phoenix activity

172 We wish to clarify some misunderstandings inherent in the often-expressed concern at 'phoenix' activity. Creditors of a business will often see it as wrong that the business can be transferred to a new corporate vehicle, leaving the creditors of OldCo with no recourse to the business for payment of the old debts. This concern is entirely valid to the extent that the assets of the business have been taken without full value having been realised (we look at that in more detail below).

173 However, to the extent that creditors complain that the ongoing revenue from the business, after the acquired assets have been fairly paid for, is unavailable to pay the old debts, we do not see it as a concern that legislation ought to address. It amounts to an argument that the creditors of NewCo

should be exposed to risk in order to ensure that creditors of OldCo are paid. This approach would be counterproductive because it would discourage investment, innovation and risk taking.

Existing mechanisms relating to phoenix activity and the need to license liquidators

174 There are many existing remedies in the Companies Act and other legislation to address the harms caused by the misuse of the voluntary liquidation process. Examples of existing provisions that help the creditors of the old company are enforcement of directors duties and fraud and dishonesty offences, repayment orders, the setting aside of prejudicial and voidable transactions and banning people from being directors.

175 While the phoenix provisions in the Companies Act are sometimes criticised for being too narrow, they do provide important protections for the creditors of the new company. Creditors of the NewCo should not be led into believing (wrongly) that the business has been longer established than it has been. The provisions themselves do not focus on the creditors of the old company.

176 What it takes for any of these mechanisms to be effective is a party to put them into action. Most of the time, this should be a decision of the liquidator based on a robust examination of the specific circumstances leading to the liquidation.

177 It therefore seems to us that the misuse of voluntary liquidations is perpetrated because the actions giving rise to the voluntary liquidation are not always investigated or investigated fully by the insolvency practitioner who may be debtor friendly, incompetent or dishonest. This would include investigating whether market value was received for assets.

178 The area of voluntary liquidations is where our key recommendation, that a licensing regime for insolvency practitioners is put into place, will make a real difference. Licensing means that liquidations will be carried out by qualified and competent professionals, bound by norms of behaviour that require that a robust liquidation process is carried out. If there are issues with the conduct of the practitioner, this can be examined and dealt with by more easily accessed and transparent complaints, investigation and disciplinary processes.

Latent defects

179 The terms of reference asked whether there is a problem with the liquidation of a company to avoid liability for latent defects. We considered this in the context of a building where, sometime in the future, a serious defect in the construction is found, such as a lack of weathertightness (a ‘leaky building’). The owners of the building are looking for redress and the company that was contracted to construct the building now does not exist, although a director of that company may be able to be found.

180 This situation almost always means that the company cannot be directly held to account for defective work that is discovered later. We understand that a common view of where insolvency law could extend is outlining circumstances where shareholders or directors, in lieu of the liquidated company, would be liable. We think it is important to recognise that limited liability (which protects shareholders) is fundamental to the success of the company form as the major legal mechanism for economic development. It provides an incentive for the aggregation of capital for a common purpose. It facilitates the use of business judgement and spreads the risk across investors and creditors. We consider that our recommendations will reduce the harm of voluntary liquidations and we have not recommended new provisions that would ‘pierce the corporate veil’.

181 Directors are not providers of capital (or at least not in their capacity as directors). As directors they should (and will) be liable if they have breached a duty that applied to them in their role of governing the company. In addition, there are existing remedies around latent defects against directors in tort. The Building Act 2004 includes a 10 year limitation period for civil proceedings relating to building

work. This means that there can continue to be legal remedies in tort against a negligent individual even if the company that was contracted to carry out the building work has been liquidated. This also means insurers have a confined period of exposure to cover.

182 There have been a small number of cases in the building sector where a director of a development company has been found personally liable in tort. Most of those successful claims have been founded on the director's control of a particular aspect of a construction project. In our view the approach that the courts have taken is generally appropriate. We do not think it is reasonable to impose a duty of care if the company director did not have sufficient control over the relevant building operation. Such a duty of care could cause governance problems when the directors are not hands-on individuals who manage and supervise the company's projects.

183 A similar scenario, not limited to the building sector, but perhaps particularly prevalent in that industry given the number of 'leaky building' claims of late, is where liquidation is seen as a response to a claim. The creditor sues or pursues the company seeking restitution. The shareholders respond by liquidating the company. The business, run by the same people, then reappears and continues to operate. Liquidation in those circumstances is seen by the creditor as the company 'avoiding' the claim.

184 But the company's response may be quite reasonable. If latent defect claims appear in such magnitude that ongoing trading, and payment of new creditors, is threatened, then it may be that liquidation is not only desirable, it is imperative. If directors cannot be satisfied that newly-acquired debt will be paid, they will be at risk of breaching the directors' duties relating to reckless trading and incurring obligations[67] if they continue trading in the OldCo. As discussed above, if a fair price is paid for the transfer of assets, the creditors of OldCo will be protected to the extent they should be protected.

185 We consider that latent defect problems in the building and construction sector are issues best solved by building and construction sector law and that this is not a problem that also needs to be, or should be, directly addressed by increasing the scope of insolvency law.

186 While we acknowledge the status quo will not always resolve all issues to the satisfaction of all of the parties, our reluctance to apply an insolvency law lens to these issues also arises from the undesirable consequences that would arise. A company should be liquidated if the most efficient use of its assets is different from the current use. We consider important objectives of insolvency law would be undermined if directors were unable to make a 'fresh start,' or if liquidations were to be delayed for several years because there was potential for latent defects to become apparent at some point in the future. The latter course would harm the New Zealand economy. It would involve removing potentially large amounts of capital from productive use and reduce liquidity in the building sector. This would create further issues such as how long the funds should be held and in what form, given they would need to be reasonably liquid, under what circumstances they would be paid out and to whom. Setting these factors out as part of the scope of insolvency law does not seem to us desirable.

Further measures

187 In addition to the contribution that insolvency practitioner licensing will make, we have three other recommendations that should be implemented regardless. These changes will help reduce the harm raised by aspects of the voluntary liquidation process.

Measure 1: Remove the ability to appoint a liquidator after service of a liquidation application

188 Currently, shareholders or directors can voluntarily appoint a liquidator up to 10 working days after service on the company of a liquidation application by a creditor.[68] This provides the opportunity to appoint a debtor-friendly, incompetent or dishonest liquidator. We recommend expanding the

[67] Companies Act, ss 135-136.
[68] Companies Act, s 241AA(2).

limitation, so that a company will be prevented from entering into voluntary liquidation from the date of service of a liquidation application by a creditor. To avoid a potential loophole, we also consider that this should apply to voluntary administrations so that an administrator cannot be appointed by the company if there is an application from a creditor already filed to appoint a liquidator to the company.

189 The insolvent company has had any time up to that point to call in a liquidator (or administrator) on its own volition. An incentive to do this earlier rather than later will be of more benefit to the creditors as a whole as more of the assets of the company will remain. The alternative processes to appoint a liquidator (or administrator) will still exist and we note that if there is regulation of insolvency practitioners, this liquidator (or administrator) will be licensed.

190 As part of this change, we recommend replacing the current ability for a petitioning creditor to apply for the court to review the liquidator's appointment with a provision enabling the shareholders to appoint a liquidator after the service of a liquidation application, but only with the approval of that petitioning creditor.[69] A further alternative would be to allow (in addition) the shareholders to apply to court for approval of the nominated liquidator. The dispute at this point is of course only as to the identity of the liquidator; both the creditor and the shareholders agree that the company should be liquidated. The ability for the creditor to apply to court to review the appointment of the liquidator made after service of the application to liquidate would no longer be required, as such appointments would not be possible without the applicant creditor's consent.

191 We considered whether our law should revert to the position under the Companies Act 1955, which remains the law in the UK. That is, in a voluntary insolvent liquidation, the appointment of a liquidator is a decision made by the creditors. They vote on the selection of the liquidator at a meeting of creditors. However, we prefer the administrative efficiency of the current approach (namely liquidator appointed by shareholders and voted on by creditors at the first meeting). The practical position would not be dissimilar to the system we have now, save that there would be many more meetings to administer as not all liquidations currently have meetings called.

Measure 2: Avoid transfers of assets after service of a liquidation application

192 At present there is no restriction on the transfer of a company's assets once a liquidation application has been filed. We consider that there should be. In our experience, the liquidation application is often the signal for a rapid transfer of assets, often at undervalue or at no value, by shareholders and directors prior to the appointment of a liquidator. This is the harm identified by the misuse of phoenix arrangements.

193 A mere prohibition on the transfer of assets would give rise to a breach of duty claim against the directors, should the assets be transferred. If the transferee had sufficient knowledge of the breach it may be required to hand back the assets. Such claims are difficult to bring, and place the onus of proof on the liquidator. We therefore prefer a provision that renders void any transfer of assets, outside the ordinary course of business, after service of the application to liquidate. The onus would then shift to the transferee to prove a basis on which it should retain the assets (such as the existing defence in section 296 of the Companies Act). If not, the liquidator would be able to recover the asset.

194 The provision would have some limits:

- It should not apply to transfers by a receiver or administrator (or by the liquidator after being appointed).
- The Court would have an ability to allow a transfer.
- The liquidator should have the ability, once appointed, to ratify the transfer.

195 Such a provision would broadly match the regime currently in place in the UK.[70] Under the UK regime,

[69] Companies Act, s 241AA(3).
[70] Insolvency Act 1986 (UK), s 127.

all dispositions of company assets after the filing of a liquidation application are void unless authorised by a court. Courts routinely receive and approve applications to allow dispositions in the ordinary course of business. We would prefer to avoid the need for repeated uncontroversial applications to the High Court, so we prefer a provision that rendered void any transfer of the company's assets other than in the ordinary course of business. That phrase is well known in the law and has a great deal of case law to explain it.

196 A transfer made outside of these restrictions will be void, so the liquidator will be able to recover the asset. However, we would expect that the existing defence in section 296 of the Companies Act would apply, so that transfers to innocent third parties could not be undone.

197 The duties of directors will still apply. A licensed practitioner will be required to turn their mind to the proper course of action.

198 The notice that accompanies the court documents in the liquidation application should contain a warning that assets must not be transferred outside the ordinary course of business.

Measure 3: Introduce a Director Identification Number

199 It can be difficult for creditors and regulators to track directors of failed companies. Our final recommendation in this area is to introduce a unique identification number for existing and future directors. This has been recently proposed for Australia by the Australian Productivity Commission in its report, *Business Set-up, Transfer and Closure*.[71] This number would be allocated after a proof of identity process and would be in addition to existing requirements. The number would be publicly available on the Companies Register.

200 As part of our recommended package of reforms, a unique identification number for each director will make it easier for stakeholders to identify and trace the activities of a director. This provides a number of benefits such as creditors being able to undertake better due diligence on a person with whom they may be considering advancing credit to. It is useful information in assessing risk, in particular for small and unsecured creditors without sophisticated resources, to have access to information that a director has multiple failed companies behind them. We also consider it will be useful for regulators to more easily identify these individuals and those who use of fictitious identities.

Conclusions on voluntary liquidations

201 Much of the harm raised by aspects of the voluntary liquidation process would be substantially reduced by licensing insolvency practitioners. Our additional recommendations to procedural rules and processes and the recommended introduction of Director Identification Numbers result in a package of reforms that, while modest on their own, overall should result in changed behaviours in this area by directors, shareholders and liquidators.

[71] Productivity Commission Report No. 75, 30 September 2015 recommendation 15.6, p.429.

Annex 1: Terms of reference

This document outlines the objectives, membership and deliverables for the Insolvency Review Working Group.

1. Objectives

The objectives of the Working Group are to:

- provide expert advice to the Minister of Commerce and Consumer Affairs (the **Minister**) on corporate insolvency law in New Zealand; and
- if appropriate, recommend possible changes to New Zealand's corporate insolvency regulatory system.

2. Background

The Companies Act 1993 and the Receiverships Act 1993 provide a menu of options, including liquidation, voluntary administration, receivership and compromises, in relation to companies that are in financial distress or may be heading towards financial distress.

The objectives of corporate insolvency law include:

- providing interested parties with appropriate incentives about whether to rehabilitate or liquidate a financially distressed company;
- discouraging directors or management from wasting the company's assets;
- ensuring all creditors of the same class are on an equal footing (i.e. the *pari passu* principle);
- providing collective debt resolution procedures that are managed by a single person;
- minimising the disruption to business activity by providing efficient insolvency procedures;
- promoting the efficient and effective operation of credit markets; and
- not undermining benefits of limited liability as a means to raise capital and encourage business risk taking and innovation.

In recent years a number of recurring issues have arisen with New Zealand's corporate insolvency law, particularly in the areas of voluntary liquidations, voidable transactions and the regulation of insolvency practitioners. A working group comprising insolvency practitioners and legal experts is being formed to investigate these issues and recommend improvements to corporate insolvency law.

3. Scope

The Working Group will provide the Minister with a report containing advice and recommendations on the matters outlined below, including analysis of the regulatory impacts of any proposed changes.

A Voluntary liquidations
Whether there are problems with voluntary liquidation of companies (including with respect to the use of phoenix companies and companies being liquidated to avoid liability for latent defects, paying arrears of wages to employees, other employee entitlements and employment related penalties) and, if so: • whether any problems are confined to the building sector or are of a general nature; • whether existing protections against abuse are effective; • whether there are sufficient incentives for parties to use available civil remedies in cases of abuse; • whether there is benefit to be able to publically search for directors of companies which have gone into liquidation; and • how any problems could be dealt with by amending company law.

B Voidable transactions and Ponzi schemes

Continue examining the voidable transaction regime and provide advice on:

- possible areas of reform of the voidable transactions regime;
- whether there are any additional issues associated with the regime and, if so, how they could be addressed; and
- any changes to company or investment law that could be proposed to aid the recovery of funds and compensation of lost funds by Ponzi scheme investors.

C Insolvency Practitioners Bill

Provide advice on whether the Insolvency Practitioners Bill should:

- be withdrawn;
- be progressed;
- have elements progressed; or
- be replaced with a licensing regime and, if so, identify the key features of the regime, how the licensing regime should be funded, and how the regime would impact on company insolvencies.

D Other corporate insolvency issues

- Identify if there are any other potential improvements to corporate insolvency law.
- Identify the main priorities for reform of corporate insolvency law.

E Implications for personal insolvency law

Identify whether there would be any implications for personal insolvency law arising from any recommendations under B and D.

Annex 2: Consideration of insolvency practitioner regulation in New Zealand

The late 1980s and early 1990s

1 The Law Commission carried out a major review of company law in the late 1980s. That review led to major legislative reform that was given effect to by replacing the Companies Act 1955 with the Companies Act 1993.

2 Corporate insolvency law was one of the many issues that the Law Commission considered. In this regard, the Law Commission's final report noted that:

> The Minister of Justice's terms of reference to the Law Commission mentioned that the Department of Justice was engaged in a review of company liquidations as part of a wider review of the law of insolvency. But the assumption that the Department's work on insolvency would be completed in advance of or at the same time as the Commission's overall work, and in close liaison with the Commission, has not come about.[72]

3 The Law Commission also referred to a major report on insolvency law that had been completed by the Australian Law Reform Commission (ALRC) in 1988. The Law Commission noted that the Australian report "has been widely applauded as a comprehensive and coherent study of the law and practice of insolvency and the direction and detail of reform in Australia… Nevertheless… there are differences between Australian and New Zealand practice and inter-related law and the Law Commission's proposals do not simply replicate those of the ALRC."[73]

4 Insolvency practitioner regulation was one area where the Law Commission recommended that New Zealand should not follow Australia:

> The Australian Law Reform Commission's proposals proceed on the premise of independent and experienced insolvency practitioners being appointed as liquidators. That reflects the existence of a system of registration of insolvency practitioners in that country. No such registration exists in New Zealand and, although it is favoured by the New Zealand Society of Accountants, the Law Commission does not feel able to recommend that such a system be established. Our consultations indicated that the idea of a regulatory system was not supported by a number of leading accountants engaged in insolvency practice nor was it supported by the current New Zealand Law Society Committee on insolvency law reform. Further, the topic of occupational regulation is currently under review by other government agencies.[74]

The late 1990s and early 2000s

5 A further opportunity to consider the regulation of insolvency practitioners arose in the late 1990s and early 2000s when the Ministry of Commerce/Ministry of Economic Development reviewed insolvency law. This review led to several major reforms including the simplification of personal bankruptcy processes, the addition of the no-asset procedure as an alternative to bankruptcy, the introduction of voluntary administration and the adoption of the *UNCITRAL Model Law on Cross-Border Insolvency (1997)*. However, work on insolvency practitioner regulation was not completed and no reforms were included in the legislation enacted by Parliament in 2006.

2006 to the present

6 The Government introduced an Insolvency Practitioners Bill (the Bill) into Parliament on 27 April 2010. The Bill, as introduced, proposed 'negative licensing'. Under this regime, the Registrar would have been able to restrict or prohibit certain individuals from providing corporate insolvency services. The Bill also

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[72] *Company Law Reform and Restatement*, Report No. 9, June 1989, at paragraph 308.
[73] ib id, paragraph 309.
[74] ib id, paragraph 643.

sought to strengthen existing provisions relating to the automatic disqualification of insolvency practitioners.

7 The Bill had a first reading on 24 August 2010 and was referred to the Commerce Committee for consideration. The New Zealand Institute of Chartered Accountants (NZICA)[75] supported negative licensing in its submission to the Commerce Committee. NZICA stated that "we believe that the proposed negative licensing regime will achieve much the same outcome as positive licensing but for less cost. The proposed negative licensing regime does not preclude moving to a full licensing regime should the proposed reforms prove insufficient."[76]

8 There was, however, considerable opposition. The Commerce Committee's report-back to Parliament noted that:

> Concerns were raised with us that the negative licensing system proposed in the bill would not address the problems and risks associated with practitioners who are dishonest, or lack independence. In line with the aim of the bill to restrict or prohibit certain individuals from providing corporate insolvency services, we consider it would be preferable to prevent such practitioners from undertaking insolvency duties before damage has been done rather than, as proposed by the bill, prohibiting or placing under supervision those who have demonstrated failure to comply with their duties.[77]

9 The Commerce Committee recommended that changes be made to the Bill to require the registration of all administrators, deed administrators, liquidators and receivers rather than a negative licensing regime. More specifically, the Committee recommended the addition of a 'fit and proper person' test, enhancing the duties of insolvency practitioners, strengthening the criteria for disqualification from appointments and specifying an appropriate range of penalties for failure to comply with statutory obligations".[78]

10 The Bill had a second reading on 7 November 2013 and is currently awaiting the Committee stage.

2013-2016: Self-regulation

11 The accreditation system introduced by CAANZ and RITANZ earlier this year was formally proposed in a consultation document issued by NZICA and INSOL New Zealand (INSOL)[79] in 2013.[80] It outlined three goals: to distinguish the quality of services provided by their members, increase public confidence in the work of members accepting insolvency engagements and assist in aligning New Zealand's regulatory framework more closely with equivalent overseas models.

12 NZICA and INSOL identified the main problem with the Bill as follows:

> [We] consider that the [Bill] as drafted will not significantly enhance the regulatory framework for insolvency practitioners in New Zealand. Indeed, it will provide persons who may be inexperienced and unqualified the opportunity to profile themselves to the public as a 'Registered Insolvency Practitioner'.[81]

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[75] NZICA has since amalgamated with the Institute of Chartered Accountants in Australia to become CAANZ. There continues to be a body corporate called the New Zealand Institute of Chartered Accountants, as required by the New Zealand Institute of Chartered Accountants Act. It is required to regulate the practice of accountancy in New Zealand with reasonable skill and care (see s 5A of that Act).

[76] NZICA submission to the Commerce Committee, 11 October 2010 http://www.parliament.nz/en-nz/pb/sc/documents/evidence?custom=00dbhoh_bill9865_1

[77] Insolvency Practitioners Bill as reported by the Commerce Committee, 9 May 2011, pp1-2, http://www.parliament.nz/resource/en-nz/49DBSCH_SCR5130_1/ff0c8795248647f2c7336a3961ffa0269c6bd0d1

[78] ib id, pp2-3.

[79] INSOL has since re-branded as RITANZ, and remains affiliated to INSOL International.

[80] *Insolvency Practitioner Regulation*, http://www.ritanz.org.nz/wp-content/uploads/Insolvency-Regulation-Consultation-Document.pdf

[81] ib id, p3.

13 The consultation document described the specific problems with the Bill in the following way:

> The Bill does not require an insolvency practitioner to have any particular qualifications or experience, nor is there any monitoring or inspection regime. Provided the person is over 18 and not otherwise disqualified, they can accept an insolvency appointment.
>
> Both NZICA and INSOL have lobbied strongly to have the Bill strengthened, without significant success and consider that the Bill does not adequately regulate insolvency practitioners. In particular, it does not provide any assurance that an insolvency practitioner is competent to practise or necessarily a fit and proper person. The Bill's proposals would move New Zealand no closer to the systems of insolvency regulation common overseas in developed countries.
>
> In addition NZICA and INSOL consider that:
>
> - Insolvency practice has become increasingly complex and specialised requiring insolvency practitioners to have a greater range of skills and expertise than has historically been the case; and
> - New Zealand insolvency practitioners are, by international standards, under-regulated. More internationally compliant regulation may facilitate greater international recognition and, at the same time, may advance the prospects of members meeting the requirements for recognition to practice in other jurisdictions.[82]

14 The consultation document also proposed an accreditation system to ensure that:

> - Insolvency practitioners have the necessary skills and experience to carry out insolvency work;
> - Insolvency practitioners are fit and proper to carry out insolvency work;
> - The sector is appropriately managed and regulated providing the public, investors and creditors with confidence in the sector;
> - New Zealand's insolvency practitioner regulation is broadly equivalent to other developed jurisdictions; and
> - New Zealand insolvencies are predominantly carried out by New Zealand residents carrying on business and with a place of business in New Zealand.[83]

[82] ib id, p5.
[83] ib id, p5.

Annex 3: Insolvency Practitioners Bill provisions not directly related to registration

1 The Insolvency Practitioners Bill proposes numerous changes to the Companies Act and Receiverships Act. These changes can be grouped into the following categories and are set out in separate tables in this Annex:

- Modifications to insolvency practitioner disqualifications
- Additions and clarifications of practitioners' responsibilities, roles and duties
- Changes relating to reporting requirements by practitioners

2 The notation 'RA' in the tables is included in the clause and section category to indicate the proposed amendment relates to the Receiverships Act. Otherwise, the section relates to the Companies Act.

3 We support all of the below amendments, except where noted otherwise. We have also suggested new amendments at the bottom of each table which would improve the functioning of the corporate insolvency system.

Table 1: Modifications to insolvency practitioner disqualifications

Item	Clause and section	Explanation of the amendment	Comments
1	cl 5 s 280	Clarifies who may not be appointed as the liquidator of a company.	We support this proposed change. It is an important and urgently-needed improvement. However, we have concerns about the language in the current proposed draft which appears intended to deal with the position of investigating accountants and similar. See paragraphs 91-96. We also recommend additional disqualification criteria to include: • ensuring that the general reference to 'creditor' includes secured creditor; • any persons who are or had been a director of a creditor company within the preceding two years before commencement of the liquidation; • any persons who had an interest in shares issued by the company or 5 per cent or more of any class of shares issued by a creditor of the company, within the preceding two years before commencement of the liquidation; • any persons who has an interest in 20 per cent or more of any class of shares issued by a related company of the company; • if there is an instrument conferring a power to appoint a receiver of a company, a person who is disqualified by the instrument from acting as the receiver of the company; and • persons (or their firms) who had a continuing business relationship with the company, or any of its directors or shareholders that have the power to appoint or remove a director of the company.
2	cl 13 s 5 RA	The amendments to s 5 of the Receiverships Act take the proposed registration system into account. They also add relatives (as defined in s 2(1) of the Companies Act) of persons disqualified under subsections 2(b) and 2(c).	We recommend also disqualifying a 'promoter or auditor of the grantor or a related company of the grantor' as an insertion to subsection (2)(b)(i). We also recommend adding two additional disqualification criteria: • If the grantor is a company, a person who has an interest, whether direct or indirect, in 20 per cent or more of any class of shares issued by a related

Item	Clause and section	Explanation of the amendment	Comments
			company. • If the property in receivership is a company, a current or former administrator, deed administrator, or liquidator of the company.
3	cl 14 s 37RA	Clarifies that the court has the discretion to determine the length of a prohibition order, including making that period indefinite. It also requires the Registrar, rather than the Official Assignee, to keep a record of any order made by the court under this section.	Currently, the court has the ability to make a prohibition order for a period not exceeding five years. Giving the court discretion to make the period indefinite aligns the Receiverships Act with the Companies Act. The Registrar leads the enforcement of the Companies Act. We agree it is more appropriate for the Registrar to keep records of any order by the court under this section.

Table 2: Additions and clarifications of practitioners' responsibilities, roles and duties

Item	Clause and section	Explanation of the amendment	Comments
4	cl 3G s 239TA (new)	Provides for documents and property to be given to an administrator's successor and creates an offence in the circumstances where the administrator does not do so.	Ensures in the event of a replacement administrator being appointed that there is an efficient transition and that the replacement administrator has all the documents and control necessary to perform their functions.
5	cl 3K s 239ABYA (new)	Requires an administrator to provide to the liquidator of a company in administration documents, information and property and creates an offence in the circumstances where the administrator does not do so.	Ensures in the event of a liquidator being appointed to a company in administration that there is an efficient transition and that the liquidator administrator has all the documents and control necessary to perform their functions.
6	cl 3L s 239ACE (new)	Introduces new steps a deed administrator must do before taking an appointment including tabling at the watershed meeting an interests statement and certifying that he or she is not disqualified from appointment.	To inform creditors of the independence of the deed administrator.
7	cl 3N s 239ACJA (new)	Requires for the documents and property to be given to a deed administrator's successor and creates an offence in the circumstances where the deed administrator does not do so.	Ensures in the event of a replacement deed administrator being appointed that there is an efficient transition and that the replacement deed administrator has all the documents and control necessary to perform their functions.
8	cl 3P s 239ACZ	Creates an offence for when the administrator fails to file an account with the Registrar as required.	The offence provision should incentivise administrators to comply with their duties. Reporting requirements aim to enhance transparency and accountability of insolvency practitioners by providing all creditors with this information.
9	cl 4 s 239ADV	Amends section 239ADV(3) to clarify that a person to whom a prohibition order applies must not act as a deed administrator of a current or other deed of company arrangement. Amends section 239ADV(4) to clarify that the court may make an order in respect of a past or current	Technical amendments to improve the clarity of the law. The Registrar leads the enforcement of the Companies Act. We agree it is more appropriate for the Registrar to keep records of any order by the court under this section.

Item	Clause and section	Explanation of the amendment	Comments
		deed administrator of a company under a deed of company arrangement. Amends section 239ADV(5) to clarify that the meaning of "failure to comply" means failure to comply with an enactment, a rule of law, or court order, to the extent that it applies to the persons in their capacity as an insolvency practitioner. Repeals section 239ADV(6). Amends section 239ADV(7) to require the Registrar, rather than the Official Assignee, to keep a record of any order by the court under this section.	
10	cl 4F s 256	Creates an offence when a liquidator fails to comply with their duties in relation to keeping accounts and records of the liquidation.	We recommend amending s 256 to require liquidators to hold accounts and records of the liquidation for six years compared with the current requirement of one year. The six year period would be consistent with the Limitation Act 2010. Introducing a six year period for keep liquidation records and accounts would also align the duties of liquidators and receivers under the Companies Act and the Receiverships Act. The current discretion of the Registrar to vary the time period should remain.
11	cl 4G s 256A (new)	Requires a liquidator to deposit funds of the company under their administration at a bank and in either a bank account to the credit of the company or a trust account. Permits the liquidator, under certain circumstances, to invest the money of a company that is not required for the time being to meet claims made against the company. All dividends, interest and other profits received from any such investments	This section would be new to the Companies Act, but has for a long time been included in the Companies Act 1993 Liquidation Regulations 1994 (regulations 37 and 38). We recommend adding an express statement that funds that are deposited in a trust account under subsection (1)(b) must be held by the liquidator on trust for the benefit of the persons legally entitled to those funds. There should be consideration of whether further regulation of such trust accounts should be better aligned with the stricter rules of relevant professional

Item	Clause and section	Explanation of the amendment	Comments
		must be paid into the bank account or trust account. Creates an offence when a liquidator fails to comply with duties in relation to company funds.	codes of practice. We expect that additional rules about the operation of such bank accounts will in due course be developed by an accredited professional organisation should our recommendation for such a licensing system be adopted.
12	cl 5C s 283	Amends section 283 to require a person vacating the office of liquidator to give written notice to the Registrar (instead of the Official Assignee). If the office of liquidator is vacant, the Registrar (instead of the Official Assignee) may appoint another practitioner or an Official Assignee as the liquidator.	This amendment is consistent with other parts of the Bill which transfers certain functions from the Official Assignee to the Registrar. We agree these transfers are appropriate.
13	cl 5D s283A (new)	Makes provision for the transfer of documents and property to a replacement liquidator and creates an offence for not doing so.	The substantive requirement is found in regulation 34 of the Companies Act 1993 Liquidation Regulations 1994. We agree with the proposal to move the obligation to the Companies Act so that an offence can be added.
14	cl 6 s 286	Adds the Registrar to the list of those able to make an application for an order to enforce liquidator's duties under section 286(1). Amends section 286(9) to require the Registrar, rather than the Official Assignee, to keep a record of any order by the court under this section.	We agree with the proposed change. The Registrar leads the enforcement of the Companies Act so it would be appropriate for the Registrar to be able to apply for an order under section 286(1) and to keep records of the orders made. We note that the orders would be made under the expanded section 284, due to our proposal to repeal section 286 of the Companies Act. See paragraphs 148-150 of our report.
15	cl 7A s 316Y (new)	This section applies to liquidators, administrators and deed administrators and sets out what must be disclosed within an interests statement and the steps a practitioner must take in preparing the interests statement.	This amendment would help identify material conflicts of interests for creditors so that an informed decision can be made about the appointment of that insolvency practitioner. We also recommend including a requirement that insolvency practitioners identify how they intend to manage any conflicts of interest identified in an interests statement.

Item	Clause and section	Explanation of the amendment	Comments
16	cl 7A s 316Z (new)	Restrictions relating to the remuneration of an insolvency practitioner. An offence is also created in relation to failing to comply with this provision.	This requirement has until now been found in the Companies Act 1993 Liquidation Regulations 1994 (regulation 29). However failure to comply is not an offence. We agree with the proposed change.
17	cl 7A ss 316ZA-316ZB (new)	Restrictions on the purchase of assets and the purchase of goods or services from a person connected to an insolvency practitioner. An offence is also created in relation to failing to comply with each provision, respectively.	This proposed change moves an existing requirement from the Companies Act 1993 Liquidation Regulations 1994 (regulations 31 and 32) to the Companies Act, and makes some appropriate changes.
18	cl 13D s 11A RA (new)	Provision for documents and property to be given to the receiver's successor and creates a new offence for failing to do so.	Ensures in the event of a replacement receiver being appointed that there is an efficient transition and that the replacement receiver has all the documents and control necessary to perform their functions.
19	cl 13E s 21 RA	Creates a new offence for a receiver failing to comply with their statutory duties in relation to money.	To prevent any mischief with respect to receivers and their statutory duty in relation to money.
20	cl 13F s 22 RA	Creates a new offence for a receiver failing to comply with their statutory duties in relation to keeping correct accounting records.	We agree with the current duty to hold accounting records that relate to the property in receivership for six years and the creation of a new offence. This is consistent with our recommendation in item 10.
21	cl 13I s 36RA	Clarifies the meaning of "failure to comply".	Ensures consistency of the terminology across the Companies Act and the Receiverships Act.
22	New	We recommend having one set of duties for all insolvency practitioners to report 'serious problems' in relation to the company. 'Serious problems' would need to have an appropriate definition. It will be necessary to afford protection to practitioners in order to encourage practitioners to report serious problems eg director duty breaches.	The current duties of liquidators, administrators and receivers to report suspected offences are problematic for the reasons given in paragraphs 102-105 of our report.

Item	Clause and section	Explanation of the amendment	Comments
		The parties that may receive the report should be expanded to include the Police, the Serious Fraud Office and the relevant authority (where appropriate), eg the Inland Revenue Department in relation to tax offences.	
23	New	Liquidators and administrators ought to include in their notices of appointment who made the appointment and if the liquidator or administrator was appointed by the court, who applied to the court for the appointment. Receivers ought to include in their notices of appointments the name of the appointing creditor, and brief details of the instrument under which the appointment was made. Deed administrators should be required to give notice of appointment to the Registrar if he or she was not the administrator. The notice of appointment should state that the appointment was made by creditors at the watershed meeting.	The Bill does not make any provisions that would require insolvency practitioners to provide in their notice of appointment to the Registrar who made the appointment. We consider that this information would be useful to creditors and would improve transparency over the appointment process.

Table 3: Changes relating to reporting requirements by practitioners

Item	Clause and section	Explanation of the amendment	Comments
24	cl 3Q s 93ACZA (new)	An administrator, at the end of an administration, and a deed administrator on termination of a deed of company arrangement, must provide a summary report to the Registrar containing prescribed information. It also creates an offence for failing to comply with this requirement.	We understand this is a report summarising the administration that would be used to collate data for statistical purposes. Prescribing what must be contained in the summary report ensures relevant information is reported on and increases the usefulness of administrator reports. The report is a useful addition as it is difficult to obtain aggregate information on insolvencies.
25	cl 4C s 234	Amends section 243(2)(a) to clarify that the liquidator must give a report, interests statement and notices to every creditor upon a meeting of creditors.	Amendment captures the new requirement for insolvency practitioners to produce an interests statement.
26	cl 4D s 245	Amends section 245(2) to clarify that when the liquidator gives notice to creditors that a meeting not be held, they must also give creditors a report, interests statement and notices to every creditor concerned.	Amendment captures the new requirement for insolvency practitioners to produce an interests statement.
27	cl 4E S 255	Amends section 255(2)(c)(ii) to require the liquidator to send an interests statement to every creditor, shareholder and the Registrar. Amends section 255(2)(d) to require the liquidator's six monthly report to be sent to every creditor and shareholder to include a statement of realisation and distribution that lists all amounts received and paid, including payer and payee details (unless inclusion would materially prejudice the exercise of his or her functions).	Amendment captures the new requirement for insolvency practitioners to produce an interests statement. The liquidator's initial report should also include more information. The intent is to enhance transparency and accountability by providing all creditors with this information. The contents of a liquidator's initial report should include: • a brief summary of the reasons for commencing the liquidation; • a summary of actions the liquidator proposes to take and estimated dates that those actions will be taken; and

Item	Clause and section	Explanation of the amendment	Comments
		Creates an offence for a liquidator failing to comply with their reporting requirements.	• a statement of the company's affairs consisting of prescribed matters. The requirements for the liquidator's six monthly report should include further information such as: • a summary of the actions taken by the liquidator since commencement of the liquidation; • details of any material changes to the actions the liquidator proposes to take; • an estimate of the completion date of the liquidation and, if different, to the previous estimated completion date, the reasons for the difference; • an updated interests statement; and • an updated state of the company's affairs consisting of prescribed matters. We recommend removing the requirement to list payer and payee details. This is an unnecessary requirement – what is important is the amount of monies distributed and how this is distributed between the different classes of creditors. Instead, therefore, we recommend that the reports be required to provide (1) details of all amounts paid to the liquidator since the commencement of the liquidation, and (2) a summary of all amounts received and paid (by and to any person) since the commencement of the liquidation.
28	cl 4H s 257	Amends section 257(1)(a) to clarify that the final report sent to creditors whose claim has been admitted and shareholders of the company must list all amounts received and paid in respect of the liquidation, including payer and payee details. In addition the clause requires the liquidator to provide to the Registrar a summary report of prescribed information. Creates an offence for the liquidator failing to	Consistent with our recommendations to clause 4E, we suggest the contents of a liquidator's final report include more information. We also agree that the liquidator must provide to the Registrar a summary report, as for our discussion of clause 3Q. The contents of a liquidator's final report should include: • a summary of actions the liquidator has taken in the liquidation; • details of all fees and other benefits paid to the liquidator; • a summary of all amounts received and paid since the commencement of the

Item	Clause and section	Explanation of the amendment	Comments
		comply with any duty in relation to the final report and accounts.	liquidation; • details of any company asset that has been disclaimed or distributed without realisation and the reasons why; • details of any company debt or liability, or class of company debt or liability, that has not been satisfied in full and the reasons why; • the extent to which unsecured creditors (preferential and ordinary) in each class were paid; and • whether there were any recoveries from creditors, directors or shareholders. Providing a cumulative report increases the amount of data publically available on the outcome of an insolvency event.
29	cl 13H s 24 RA	Amends section 24 and clarifies what must be contained in the receiver's six monthly report and the final report.	Consistent with our recommendations to improve liquidator reporting requirements and to enhance transparency and accountability to creditors, we recommend that six monthly and final receivership reports should include the following information: • details of each amount received and paid in respect of the receivership since the receiver's previous report; • details of property disposed of since the date of any previous report and any proposals for the disposal of property in receivership; • details of all fees, allowances, reimbursements, or other benefits paid to the receiver since the commencement of the receivership; • a summary of all amounts received and paid in respect of the receivership since the commencement of the receivership; • details of amounts owing, as at the date of the report,— • (i) to any person in whose interests the receiver was appointed; and • (ii) to creditors of the grantor having preferential • claims; • details of amounts likely to be available, as at the date of the report, for

Item	Clause and section	Explanation of the amendment	Comments
			payment to creditors other than those referred to in paragraph directly above; and • the state of affairs with respect to the property in receivership as at the end of the period.
30	cl 13HA s 24A RA (new)	A summary report at the end of the receivership is to be given to the Registrar and creates an offence for not doing so.	We also agree that the receiver must provide to the Registrar a summary report, as per our discussion of clause 3Q.

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