Impact Summary: Funding the provision of independent oversight of the insolvency practitioners regime

Section 1: General information

Purpose
The Ministry of Business, Innovation and Employment (MBIE) is solely responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing final decisions to proceed with a policy change to be taken by or on behalf of Cabinet.

Key Limitations or Constraints on Analysis
There are no limitations or constraints on our analysis as to which persons within the corporate governance regulatory system should be charged for the provision of independent oversight of the insolvency practitioners regime, by the Companies Office.
Responsible Manager (signature and date):
1/3/19 Susan Hall Manager, Business Law Commerce, Consumers and Communications Branch Ministry of Business, Innovation and Employment

Section 2: Problem definition and objectives

2.1 What is the policy problem or opportunity?
In November 2016, Cabinet decided that a co-regulatory licensing regime would be introduced for insolvency practitioners. One of the consequences of this decision is that the Companies Office would need to be funded to provide independent oversight of this regime. This was brought to Cabinet's attention in 2016. In that paper the Minister of Commerce and Consumer Affairs: • proposed that this would be funded through the annual return fee for companies • indicated that he intended to make a Budget bid in 2017 to seek an appropriation for independent oversight, to be funded through the annual return fee for companies. These decisions presuppose that the cost of independent oversight would be spread across all companies. This approach was premised on the misunderstanding that fee revenue collected under the Companies Act could be used for functions unrelated to the purpose for which it was collected. However, we now understand that the use of fees collected to under the Companies Act to fund the Registrar of Companies' oversight activities would be outside the scope of the fee setting powers in the Companies Act. It is therefore necessary to consider what alternative funding source should be put in place to enable the Companies Office to perform its oversight function.

2.2 Who is affected and how?
The decision on how the Companies Office will be funded to perform its oversight function will impact the persons who are required to meet this cost i.e. all companies. Different options will impact on the amounts individual payers will pay each year.

2.3 Are there any constraints on the scope for decision making?
Yes. The Cabinet decisions obtained in 2016 presuppose that the cost of independent oversight will be wholly funded from within the corporate governance regulatory system. On that basis, Crown funding is not an option and we have not explored that option.

Section 3: Options identification

3.1 What options have been considered?

We considered six options for recovering the costs of independent oversight from with the corporate governance regulatory system.

These options are a combination of two questions about who to charge and how to charge them.

		How to charge	
		Fee	Levy
Who to charge	Insolvency practitioners	A. Charge a fee to all insolvency practitioners for the provision of independent oversight	B. Levy all insolvency practitioners for the provision of independent oversight
	Split between Companies and insolvency practitioners	C. Charge a fee to both insolvency practitioners and Companies for the provision of independent oversight	D. Charge a levy to both insolvency practitioners and Companies for the provision of independent oversight
	Companies	E. Charge a discrete fee to all companies for the provision of independent oversight	F. Levy all companies for the provision of independent oversight **(Our preferred Option)**

Under each option all companies benefit from the provision of independent oversight of the insolvency practitioners regime as, as a result of that oversight:

- all businesses benefit from improving and maintaining the integrity of the insolvency regime; and
- most businesses are creditors of other businesses and so would benefit from improved practices in the way businesses are liquidated and the way creditors are paid.

3.2 Which of these options is the proposed approach?

Option F is the proposed approach. We discarded those options which involved charging insolvency practitioners directly and those which used fees. We did this for the following reasons:

Why we discarded charging insolvency practitioners directly (Options A, B, C & D)

Options A and B could harm competition and have resourcing implications for the Crown
In 2016, when a RIS was prepared to accompany the 2016 Cabinet decisions we estimated that the annual cost for a government regulator to provide independent oversight of insolvency practitioners would cost around $750,000-$1,000,000.

This estimate is based on Financial Markets Authority's experience under the *Auditor Regulation Act 2011*, in which auditors are regulated under a co-regulatory model.

The size of the audit profession is approximately 100 practitioners, similar to the insolvency services market. If costs were to be recovered from the profession in the form of fees and/or levies, this would mean that the costs per practitioner would be approximately $7,500-$10,000 per year. As it is intended that licences will be granted for 5 year periods, recovering 5 years worth of costs would result in licensing fees in the order of $37,500 to $50,000.

A licensing fee in this order of magnitude could drive some smaller practitioners out of the market. This would:

- harm competition by reducing the number of practitioners available to take appointments; and
- the reduction in the number of practitioners available to take appointments could have fiscal implications, as the Crown (through the Official Assignee) acts as a liquidator of last resort. This would require the Official Assignee to perform a larger number of liquidations where there are insufficient assets available to complete the liquidation.

Those costs would likely be passed on to creditors – increasing their losses
Insolvency practitioners are likely to seek to recover their registration costs from the fees they charge. These fees are met from the remaining assets of an insolvent business - before any money is paid to creditors and in particular, unsecured creditors.

We expect that the amount of that increase would be low on a per creditor basis.

Insolvency practitioners will be required to meet the costs of front line regulation
The proposed insolvency practitioners regime is a co-regulatory one, with a front line industry regulator and a second line government regulator.

Insolvency practitioners will be required to fund (through membership fees etc.) the costs of the front line regulator for this regime.

The industry body which we expect will become the front line regulator (Chartered Accountants Australia New Zealand) currently charges insolvency practitioners $250 per year to become "accredited". We expect that this fee will increase materially once the licensing regime comes into effect.

It would be inconsistent with the policy underlying the Cabinet decisions in 2016
The Cabinet paper in 2016 specifically considered and rejected the option of charging insolvency practitioners, in favour of charging all companies.

A problem has been identified with the specific mechanism identified in 2016 for spreading the costs of independent oversight across all companies. However, the Cabinet decisions establishing the independent oversight regime (and the funding decisions made at that time) presuppose that the cost of independent oversight would be spread across all companies.

Charging insolvency practitioners would be inconsistent with the policy underlying those decisions.

Why we discarded the options for recovering the costs of oversight through fees (Options A,C & E)
The difference between a fee and a levy is discussed in guidance produced by the Treasury, the LDAC, and the Auditor-General.[1] Essentially the difference between a fee and a levy is that a fee is a charge that relates to specific goods or services provided to an individual, whereas as a levy is a charge to a certain group for a particular purpose (i.e. where the benefit of any good or service that is provide through fulfilment of the purpose is more difficult to ascribe to any particular individual).

The nature of the two charges is quite different. A levy is considered to be akin to a tax. Taxation must be clearly authorised in primary legislation, or by regulations authorised by such legislation (section 22(a) of the Constitution Act 1986). A fee is not considered to be taxation, but is rather a charge for the direct provision of goods or services.

We do not consider that it is credible to characterise the proposed oversight functions of the Registrar of Companies as a charge to companies for the direct provision of a service ie a fee.

The Regulations Review Committee has also previously considered and identified conceptual challenges with using fee revenue to fund an enforcement function in other contexts.

Most fee payers (companies) will likely never interact with the Registrar of Companies in its capacity as the regulator of the Insolvency Practitioners regime, so it is hard to characterise this function as the provision of a service to those companies which can be charged for.

The regulation of insolvency practitioners will also provide a benefit to the general public – it is not only companies that benefit from the regulation of insolvency practitioners.
Non-company creditors can also derive benefits from the improved regulation of the insolvency practitioner regime and the improved practices in the way businesses are liquidated and the way creditors are paid

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[1] LDAC *Legislation Guidelines 2018 Edition*, Treasury's *Guidelines for Setting Charges in the Public Sector* (2017), and the Office of the Auditor-General's guidance *Charging fees for public sector goods and services* (2008).

Funding of the Registrar of Companies' oversight functions by way of a levy would therefore appear, consistent with guidance produced by the Treasury, the LDAC, to be the appropriate mechanism, given that third-party funding has been chosen as the method for funding the Registrar's functions (as opposed to general taxation). This is particularly the case given that no specific output is being provided to companies for which they can be charged a fee.

We note that the amount charged to companies would not change under either option.

Our preferred option

For the reasons set out above, our preferred legislative option for funding the Registrar of Companies to provided independent oversight of the Insolvency Practitioners regime is to put in place a mechanism to charge a levy to all companies (**Option F**).

Section 4: Impact Analysis (Proposed approach)

4.1 Summary table of costs and benefits

Affected parties *(identify)*	**Comment:** nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks	**Impact** *$m present value, for monetised impacts; high, medium or low for non-monetised impacts*
Additional costs of proposed approach, compared to taking no action		
Regulated parties	Companies will be expected to meet the costs of providing independent oversight.	There are presently approximately 600,000 companies. Based on the expected cost of independent oversight the charge to individual companies (around $750,000-$1,000,000) will be between $1.25 and $1.67 each year
Regulators	-	
Wider government	-	
Other parties	-	
Total Monetised Cost	$750,000-$1,000,000 (between $1.25 and $1.67 per company)	
Non-monetised costs	*Low*	*(High, medium or low)*
Expected benefits of proposed approach, compared to taking no action		
Regulated parties	Our preferred option will spread the cost of independent oversight across the largest number of parties resulting in the smallest individual charge.	-
Regulators	This option will provide the Companies Office with a reliable and regular funding stream to provide oversight functions.	-
Wider government	-	
Other parties		
Total Monetised Benefit	-	
Non-monetised benefits	Medium	*(High, medium or low)*

4.2 What other impacts is this approach likely to have?

Nil.

Section 5: Stakeholder views

5.1 What do stakeholders think about the problem and the proposed solution?
The great majority of submitters on SOP No. 45 to the Insolvency Practitioners Bill were in favour of independent oversight. However, as the imposition of a levy on all companies was not part of that SOP submitters did not have the ability to comment on how it would be funded.

Section 6: Implementation and operation

6.1 How will the new arrangements be given effect?
The preferred option would be given effect by way of an SOP to the Insolvency Practitioners Bill at the Committee of the Whole House. The Companies Office will be responsible for determining the amount of the levy to be imposed on companies. The amount of this levy will then be adjusted as part of the periodic Companies Office fee review process, which includes a requirement to consult with affected parties. We anticipate that the levy would: • Be collected from companies at the same time they file their annual return (both the FMA and the External Reporting Board collect a portion of their funding in this way). • Begin being collected from 1 July 2020 – when we anticipate that the insolvency practitioner regime would come into effect.