# Capability review of the Australian Securities and Investments Commission

We comment on only one of ASIC’s operations, that is, its regulation and coverage of corporate insolvency practitioners.

In that respect, we note that the Minister says that, in assessing ASIC’s approach to its statutory objectives, the review may provide observations, but not make recommendations on ASIC’s regulatory framework or powers. We observe, as have others[[1]](#footnote-1), that the regulation of the insolvency profession by ASIC fails in many ways and that it represents one area where ASIC should be relieved of its regulatory burden. The reasons for this are articulated below.

**Insolvency Context**

Insolvency is a discipline based on principles extending historically to Roman times and earlier. It originally manifested, necessarily, in personal bankruptcy and then extended to companies in the 19th century.

There are fundamental principles of insolvency processes that are common to both personal and corporate insolvency notwithstanding the nature of the company as an artificial body. In Australia too many aspects of the insolvency process are differentiated. So despite the similarity of the processes, there is separate legislation, separate regulators, separate courts and the government departments and Ministers are different. Differences also exist in the government support and involvement.

We are not recommending wholesale change in this structure, for practical and legal reasons it would be too hard to achieve – but we do recommend that aspects of this division be attended to. These are shown in this table.

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| --- | --- | --- | --- |
|  | **Personal insolvency** | **Corporate Insolvency** | **Proposed** |
| **Regulator** | AFSA | ASIC | new |
| **Law** | Bankruptcy Act 1966 | Corporations Act Ch 5, 2001 | As is |
| **Department** | AGD | Treasury | As decided |
| **Minister** | A-G | Assistant Treasurer | As decided |
| **Courts** | Federal and Federal Circuit Court | Federal and Supreme Courts | As is |
| **Government support** | Official Trustee in Bankruptcy | No | As is |

There are some linkages allowing our recommendation to be implemented. For example, apart from the legal and administrative structure, the insolvency profession is itself cohesive, in the sense that many liquidators are also trustees, and its education and training covers both. There is the one professional body, ARITA. There are often bankruptcies of directors of companies in liquidation. Specialist texts and publications tend to cover both personal and corporate insolvency.

**The problem**

The essential problem is that ASIC regulates corporate practitioners, and a separate body, AFSA, regulates personal insolvency practitioners. The standards and practices of each discipline are largely common, but are kept divided by the separate approaches taken by these regulators.

This raises the issue of the regulatory burden, which is a cost ultimately borne by all businesses and consumers. Given that the revenue authorities are often involved as creditors in insolvency, in both personal and corporate, the cost is borne directly by the broader society as well.

In so far as you are examining ASIC’s capability, we submit that while it may be ‘capable’ as an insolvency regulator, insolvency regulation would benefit by its removal from ASIC’s responsibilities. The focus should not be on ASIC, or AFSA, but the beneficial regulation and support of the insolvency profession.

We recommend this given that insolvency itself is only a very minor part of ASIC’s authority. The lack of policy and law reform attention to corporate insolvency has suffered as a result.

Further we posit that ASIC does not take an effective and appropriate approach to the regulation of insolvency practitioners who are regulated without regard to their particular legal authority, responsibilities and duties.

**Liquidators**

Liquidators are unlike other regulated entities of ASIC. They are officers of the court, to which they are answerable; liquidators have significant responsibilities and duties under the law and significant powers and discretions. Liquidators can demand information, conduct compulsory examinations, take legal proceedings not available to other litigants in the conduct of which they are held to high standards approaching that of a model litigant. They are not permitted to take advantage of strict legal rights if this would unjustly enrich the insolvent estate (‘the rule in ex parte James’). They act quasi-judicially in assessing creditor claims.

“The office of a person appointed liquidator to a corporation, does not fit any precise legal category or classification, which defines the rights and liabilities, attaching to that office. It is a hybrid composite with elements of fiduciary, trustee, agent, officer of the corporation and (in some instances) "officer" of the Court. Attached to those elements are the obligations along with the powers and discretions which apply to those roles”.[[2]](#footnote-2)

Importantly, they have statutory duties to investigate and report unlawful conduct to ASIC, and to assist in the pursuit of prosecutions. ASIC appoints liquidators in cases of corporate fraud. Indeed in its Regulatory Guide 16 for external administrators, ASIC states that external administrators ‘are the front-line investigators of insolvent corporations’.

Liquidators can be required to assume personal liability for debts incurred by a company in administration; they are required to attend to work done even without remuneration; and they have a complex legal status beyond that stated in the legislation.

Liquidators in Australia at least, operate in a unique environment, with no government liquidator available for the winding up of insolvent assetless companies. While liquidators are entitled as trustees to be remunerated from trust assets, insolvency inherently involves limited or no assets. Where assets are available, creditors’ returns are necessarily impacted by their remuneration.

We consider ASIC’s current regulation of liquidators does not acknowledge the particular legal status of liquidators or the environment in which they work. Rather liquidators are subject to ASIC “surveillance” and regulated in ASIC’s “law enforcement” role, as if a liquidator were any type of market or business participant.

That is not a valid primary focus for the regulation of liquidators, any more than it is to speak of comparable statutory office holders – tribunal members, appointees to statutory roles - in that way.

Overall, ASIC’s focus on insolvency is necessarily limited, given the large number of its other responsibilities, and its approach is tainted by its rather singular approach to its “legal enforcement” role. Its annual reports contain limited information, referring to liquidators as one of its “gatekeepers”, along with directors and product manufacturers and distributors.

Rather than proceed further by way of comment on ASIC’s approach to its insolvency role, we compare it with the regulatory approach taken in personal insolvency by the Australian Financial Security Authority (AFSA).

AFSA has come to its position as what we consider to be an effective insolvency regulator from its long history of focusing on insolvency, and its actual practice of that discipline, through the Official Trustee. What we consider is its greater effectiveness and better approach is now explained.

**AFSA Comparison**

AFSA as an organization both practises as a trustee, through the Official Trustee in Bankruptcy, and regulates the trustee profession, through its Regulation Unit. The Official Trustee itself is regulated by AFSA;

AFSA adopts what we consider to be a co-regulatory model with the trustee profession, with an approach transparently explained in its various regulatory guidance: see its Insolvency Practitioner Compliance Program 2015-2016. It refers to a regulatory approach which “focuses on early resolution of systemic issues by adopting a proactive and preventive approach wherever possible”, and in the accepted enforcement pyramid, commencing “on the basis of working cooperatively with practitioners using supportive regulatory strategies”, but at the same time applying focused risk management approaches to its regulation.

Given the inherent nature of insolvency, involving the balance between the public interest and the limited funds available, there is a co-resourcing approach - enlisting trustees to assist with AFSA’s work overflows, through AFSA’s national trustee panel; and under a legal regime where AFSA itself assists trustees in estate administrations – for example, AFSA issues statutory demands for information and conducts examinations on behalf of trustees, under s 77A and 139ZQ. Importantly, AFSA takes on the responsibility to enforce bankrupts’ obligation to provide a statement of affairs, a fundamental source document required by trustees, under s 77C.

AFSA publishes extensive guidance, both as to principles and practice, on which it often consults the profession.

Its forms and processes undergo continuous review. As one comparison with ASIC, the statement of affairs form of AFSA has been continually refined as needs change, and AFSA contemplates its on-line filing. The report of affairs of ASIC dates back decades, and despite a major 2011 report on its deficiencies, is yet to be reformed.

AFSA provides a collaborative offence referral arrangement, the pre referral enquiry process, PRE, to facilitate offence referrals.

AFSA has also embraced the need for streamlined approaches, with virtual meetings of creditors, and online payment of statutory charges and reporting. Its regulatory approach is increasingly technology based, in particular its eInspections, by which trustees’ files can be reviewed on line. Its new AER Online provides easy access for trustees to on-going information.

AFSA’s regulatory efficiency is well beyond that of ASIC. Indeed its further planned online approach is consistent with the FSIR recommendations, that regulators adopt technology based processes.

AFSA has taken on responsibility for the large amount of data it accumulates, engaging a statistician to report regularly. These allow reporting on the costs and efficiency of the personal insolvency regime. This informs policy debate and change. We can assess the assets available in bankruptcies, their realization costs, the amount of creditor claims, the costs of government and other charges, and the ultimate dividend return. Comparisons can be made with other types of personal insolvency administration.

Much less of this information is available in corporate insolvency.

AFSA’s influence on beneficial development of the legal regime is evidenced by the extensive reforms to the Bankruptcy Act, addressing fundamental issues such as debt agreements (1996 and 2007), personal insolvency agreements (2004), family law (2005), superannuation (2006) and creditor petitions (2010). In contrast, the major corporate insolvency reforms of 1993 were next followed fifteen years later by those in 2008, which while important were not fundamental. Nearly all reforms proposed since then have not been given attention. The unduly complex Insolvency Law Reform Bill 2013, followed by the next version of 2014, has still not proceeded.

**Conclusions**

The need for harmonization of insolvency laws and practices dates from at least the Harmer Report of 1988. More recently, the Senate Economic References Committee Report of 2010[[3]](#footnote-3) recommended the establishment of a single regulator, the AIPA. The Productivity Commission Report of 2010[[4]](#footnote-4) further recommended harmonization as a matter of efficiency.

The benefit for ASIC would be that it would be relieved of a discipline that does not sit well with the other market participants it regulates. The need for ASIC to separately maintain expertise in insolvency would be removed. The need for ASIC and AFSA to both regulate the one practitioner would be avoided.

And the telling need for clauses 10-5 in the Insolvency Law Reform Bill 2014 to require ASIC and AFSA to “work co-operatively” with each other would not be needed.

Had the 2010 Senate report recommendation been implemented, we consider that the disparity of approach between these regulators would not exist, or to the same extent. If ASIC were to continue to retain its insolvency role, we cannot see any real prospect of the harmonization that is needed. It is not culturally capable of doing so.

Also relevant to our submission is the review of ASIC’s funding model. We consider that applied by AFSA is appropriate; or in any event the two insolvency regulators should not have separate funding approaches.

We have only cited limited references to our statements. We can substantiate and refer you to more detailed commentary, sections if required, for all of the issues in this submission.

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1. Economic References Committee Australian Senate, *The regulation, registration and remuneration of insolvency practitioners in Australia: the case for a new framework,* September 2010. [↑](#footnote-ref-1)
2. *Sydlow Pty Ltd (In Liquidation) v T G Kotselas Pty Ltd, Theo George Kotselas and William James Hamilton* [1996] FCA 1384 at [26] [↑](#footnote-ref-2)
3. Economic References Committee Australian Senate, *The regulation, registration and remuneration of insolvency practitioners in Australia: the case for a new framework,* September 2010; see specifically Chapter 10 and particularly [10.3] to [10.17]. The Report concluded [at [11.5] *that regardless of funding, ASIC is overburdened* [↑](#footnote-ref-3)
4. The Productivity Commission, *Annual Review of Regulatory Burdens on Business: Business and Consumer Services*, August 2010, stated at p175 ‘*In parallel with the deliberations of the reform taskforce that the Commission has proposed, the Government should re-examine the case for making a single regulator responsible for both areas of insolvency law, including the registration of insolvency practitioners.’* [↑](#footnote-ref-4)