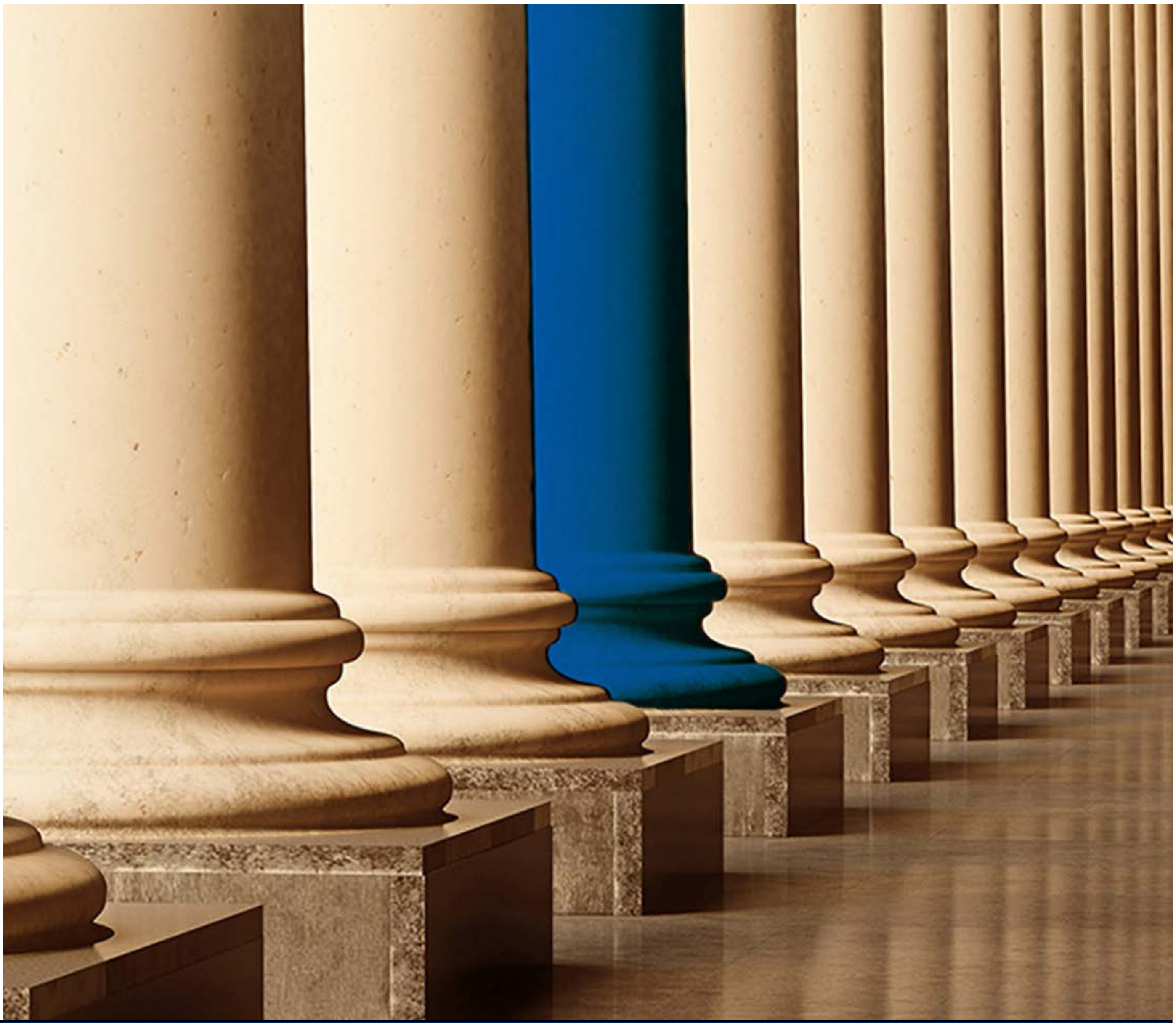

Insolvency Practitioners Bill 2010: Submission on Supplementary Order Paper No. 45

24 August 2018

BELL GULLY

Introduction and overview

This submission on Supplementary Order Paper No. 45 is made by Bell Gully.

About Bell Gully

Bell Gully has a wealth of expertise and experience in insolvency, corporate restructuring, receiverships, administrations, and liquidations. The practice is built around the multi-disciplinary expertise of experienced and highly regarded finance, litigation and corporate specialists. Our specialist team is regularly engaged to assist receivers, administrators, liquidators, other insolvency practitioners, and creditors, across the broad range of insolvency and restructuring matters.

Approach to this submission

The views in this report are our own, and do not necessarily represent the views of any of Bell Gully's clients.

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Overarching comments

Overall, we support the changes proposed by Supplementary Order Paper No. 45 (the **SOP**). In particular, we support the proposed model for the regulation and supervision of insolvency practitioners. In our view it provides a better balance than the previous proposals between the need to set and enforce clear qualification and performance standards, and the desire not to unduly restrict the freedom of competent practitioners to act.

We comment on particular aspects of the SOP below.

Duty of care: Clause 3R / Proposed section 239ADUB Companies Act 1993; Clause 5E / Proposed section 285A Companies Act 1993; Clause 13I / Proposed section 36A Receiverships Act 1993

The SOP proposes that (in summary) any party who has or is likely to suffer loss or damage as a result of a "failure to comply" by a liquidator, administrator, or receiver acting in that capacity may apply to the Court for remedial orders, including orders that the insolvency practitioner compensate the aggrieved party for their loss or damage. "Failure to comply" is defined very broadly, and includes any failure to comply with any enactment or "rule of law".

Although we understand the desire to ensure that there are effective mechanisms to address any poor performance by insolvency practitioners, we do not support the introduction of these sections. We consider that the practical issues they will create outweigh their potential benefits.

The issue arises because of the breadth of the right to seek relief, especially compensation. In particular:

(a) The definition of "failure to comply" is broad. It will include a failure to comply with "any enactment". As well as the many specific duties imposed on insolvency practitioners, this will include, for example, the general obligation to realise and distribute the assets of the company in a "reasonable and efficient manner" (s 253 Companies Act 1993). It also includes a failure to comply with any "rule of law". This is likely extend to any general common law duties of care.

(b) The Act empowers the Court to make "any order it sees just" if there has been a failure to comply, including orders that the insolvency practitioner make compensation to an aggrieved party.

The common law and the existing legislation both provide well-understood limits on the circumstances in which a failure to comply with legislation, or a failure to take reasonable care, can result in liability to compensate aggrieved parties. In our view, departing from those established principles and creating a new and generalised judicial discretion risks considerable uncertainty. It is unclear which categories of aggrieved person might be awarded compensation, and for what types of loss, and what connection the loss must have with the failure to comply in order for an award to be just. Whatever the standard, it is likely to depart from the tests established at common law.

The risks posed by such uncertainty are particularly acute in the insolvency context, in which some stakeholders will by definition suffer a shortfall or a loss. Those circumstances naturally increase the risk of claims being made, including when the merits of a claim are unclear. This can be seen in the context of existing rights of action. For example, it is not an uncommon experience for mortgagees to face claims that they have sold mortgaged property for less than the best price reasonably obtainable at the time. There is now a clear standard for assessing these claims. It is much less clear how a general right to seek compensation would be applied, especially in circumstances where compliance cannot readily be assessed by reference to a clearly-articulated process (as is the case with the sale of mortgaged property). This poses real issues for insolvency practitioners when deciding whether to accept appointments, and how to conduct them. It also risks diversion of resource to deal with unmeritorious or uncertain claims.

Accordingly, on balance, we do not support the inclusion of these sections.

Continuing business relationship disqualification: Clause 5 / Proposed section 280 Companies Act 1993

The proposed s 280(3)(a) provides that a person is not disqualified under s 280(2)(d) if in the two years prior to liquidation the person had been appointed "to investigate or advise on the solvency of the company", in certain circumstances. This is narrower than the previously proposed section, which would have related to a person appointed to "investigate, monitor, or advise on the affairs of the company". The previous formulation appears to have been intended to align with the definition of "continuing business relationship in paragraph 9 of the Insolvency Engagement Standard.

The change in the drafting is likely to be interpreted as meaning that an engagement to monitor or advise on the affairs of a company nearing insolvency, rather than one limited to investigating the solvency of the company, will not fall within the exception.

In that context, we suggest that the exception in its current form is unduly narrow. Many typical pre-liquidation may extend beyond merely monitoring or advising on solvency issues, and the practitioners that accept those appointments will often be the most familiar with the business of the company and the most suitable for appointment as liquidator.

Related creditor voting: Clause 3HA / Proposed sections 239AM Companies Act 1993 et seq; clause 4DA / proposed section 245A Companies Act 1993 et seq

Proposed sections 239AM, 239AMA, 239AMB, 245A, 245B,and 245C relate to related party voting at creditors' meetings during administrations and liquidations respectively. They provide that related creditors' votes must be disregarded at creditors' meetings.

We support the policy underlying these changes. Minor changes may improve the way the sections operate in practice. In particular:

(a) New sections 245C(2) and 245C(4) (and s 293AMB(2) and 239AMB(4)) address the situation where a related creditor has voted on a resolution and redress is sought from the Court. There is no equivalent provision for the situation where a creditors' votes are not taken into account (rightly or wrongly) and an application is made under s 245A or s 245B. We recommend including analogous provisions in those sections.

(b) The sections require and permit certain conduct by the "liquidator" or "administrator" respectively. It is not clear how they operate when the effect of a vote has been to remove an administrator or liquidator. In particular, if displaced former administrators or liquidators are intended to have standing to make an application then we suggest that be made explicit in the section.

Restriction on appointment of liquidator: Clause 4BB / Proposed s 241AA Companies Act 1993

Proposed section 241AA of the Companies Act 1993 would provide that if a creditor has applied for orders to liquidate a company then a liquidator may be appointed by the shareholders (under s 241(2)(a)) or directors (under s 241(2)(b)) only with that creditor's consent.

On balance, we do not support this proposed change. In particular:

(a) The fact that the prohibition operates from when the application is filed, rather than when it is served, means that shareholders and directors will have no way of knowing whether or not the prohibition applies to them (until they are served with an application). There may also be evidential difficulty establishing which event took place first in time, in some circumstances. This uncertainty is undesirable as it leaves both liquidators and directors in an uncertain position during a time when prompt action may be required.

(b) More generally, on balance, there is a risk that the prohibition will do more harm than good. It appears to be intended to prevent directors or shareholders from appointing their preferred liquidator in circumstances where the appointment of a liquidator chosen by a creditor is foreseeable. In our view:

   (i) This type of appointment is problematic to the extent it is assumed that the liquidator preferred by the shareholders or directors is unlikely to perform his or her function as diligently or competently as the individual proposed by the creditor. If the SOP becomes law, this concern will be less acute. Insolvency practitioners are licensed and subject to regulatory oversight, and, especially if the proposed "failure to comply" provisions are enacted, there will be a ready means of redress for creditors if the liquidator does not perform. Accordingly, the mischief being addressed by the section is already substantially addressed by other parts of the SOP.

   (ii) At the same time, the section may limit or complicate legitimate and necessary appointments. Directors will be put in a difficult position if they consider that a company is insolvent and that a liquidator should be appointed, but there is a bona fides dispute with one creditor about the identity of the liquidator. In those circumstances the better outcome may be to allow the directors to make the appointment and to allow creditors to address the appointment at a creditors' meeting if they decide to do so.

Accordingly, especially in circumstances where related party votes are excluded from voting at the creditors' meeting, we consider there is a risk that the proposed section is unnecessarily restrictive.