

## **DISCIPLINE AND REMEDIAL SUPERVISION**

8.1. In this chapter, the various mechanisms for dealing with the conduct of registered liquidators in relation to particular matters are considered. In particular, the two types of disciplinary procedures (statutory and self-regulatory) are considered as well as the various powers of the ASC and the courts to investigate conduct, make remedial orders and related matters.

### **DISCIPLINARY PROCEDURES**

8.2. There are essentially two separate procedures which may be used in relation to disciplining corporate insolvency practitioners. The first is a 'registered liquidator specific' statutory procedure involving the ASC, the CALDB and the AAT. The second comprises the self-regulatory procedures set down in the internal rules of the professional bodies which are not designed specifically for corporate insolvency practitioners.

#### **The Statutory System: ASC/CALDB/AAT**

8.3. The CALDB is established under the ASC Law.<sup>1</sup> Its membership consists of a Chairperson (who is a legal practitioner) and two other members selected by the Minister from panels of five persons nominated by each of the ICAA and the ASCPA.<sup>2</sup>

8.4. Upon an application by the ASC, the CALDB is empowered under the Corporations Law to suspend or cancel a registered liquidator's registration if it is satisfied that the liquidator:

- has failed to comply with the requirements to lodge triennial statements;
- has ceased to live in Australia;

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<sup>1</sup> Section 202 ASC Law.

<sup>2</sup> Section 203 ASC Law.

- has failed to carry out or perform adequately and properly the duties of a registered liquidator; or
- is otherwise not a fit and proper person to remain a registered liquidator.<sup>3</sup>

Similar powers exist in relation to liquidators of specified bodies corporate.<sup>4</sup>

8.5. Where the ASC's application relates to a liquidator's failure to adequately or properly carry out or perform his or her duties, or the unfitness of the person to remain a registered liquidator, the CALDB is given additional powers to deal with the person by:

- admonishing or reprimanding the person;
- requiring the person to give an undertaking to refrain from engaging in certain conduct; or
- requiring the person to give an undertaking to refrain from engaging in certain conduct, except on specified conditions.<sup>5</sup>

If a person fails to give an undertaking as required, the CALDB may cancel or suspend the person's registration.

8.6. The CALDB's powers may be exercised whether or not the conduct in question constituted, or may have constituted, an offence, and whether or not any proceedings are brought in relation to the conduct.<sup>6</sup>

8.7. Proceedings of the CALDB are intended to be conducted with as much expedition and as little formality and technicality as possible.<sup>7</sup> However, the CALDB is still required to observe the principles of natural justice.<sup>8</sup> In particular, the CALDB must not make any orders or otherwise deal with a person unless it has given the person concerned an opportunity to be heard in relation to the matter.<sup>9</sup> It must also give the ASC an opportunity to appear.<sup>10</sup>

8.8. The CALDB is required to provide the liquidator and the ASC with written reasons for its decisions and to publish notices of its decisions in the *Commonwealth*

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<sup>3</sup> Subsection 1292(2), Corporations Law.

<sup>4</sup> Subsection 1292(3), Corporations Law.

<sup>5</sup> Subsection 1292(9), Corporations Law.

<sup>6</sup> Subsection 1292(11), Corporations Law.

<sup>7</sup> Subsection 218(1) ASC Law.

<sup>8</sup> Subsection 218(2) ASC Law.

<sup>9</sup> Subsection 1294(1), Corporations Law.

<sup>10</sup> Subsection 1294(2), Corporations Law.

of *Australia Gazette*.<sup>11</sup> Decisions of the CALDB are subject to review by the AAT at the instigation of the ASC, the liquidator concerned, or any other affected person.<sup>12</sup>

8.9. There have been few instances where conduct of liquidators has been referred by the ASC to the CALDB. According to the CALDB's latest annual report, from its establishment in 1991 to June 1996 there had been only nine referrals involving registered liquidators, and four of the persons involved were also registered auditors.<sup>13</sup> In 1995–96, only two liquidators were referred to the CALDB.<sup>14</sup>

8.10. As mentioned above, at present, only the ASC may refer matters to the CALDB. The figures indicate an apparent reluctance on the part of the ASC to do so. In this regard, it is understood the ASC has some concerns that proceedings before the CALDB are conducted in a manner which is too legalistic and consequently too expensive to prepare for.

8.11. In its 1994–95 annual report, the CALDB highlighted its own concerns about the lack of referrals.<sup>15</sup> In particular, the CALDB expressed concern about the manner in which matters were presented to it by the ASC. The CALDB also noted that it had introduced a pre-hearing conference procedure and a mediation facility in an effort to streamline the process. In this regard, the CALDB has asked for amendments to its enabling legislation to clarify its powers in this area.

8.12. Practitioners who are members of the ASCPA, the ICAA or the IPAA are bound by the codes of conduct and ethical standards of their respective bodies. These codes require members to apply relevant professional pronouncements when undertaking insolvency work. The Articles and By-laws of the organisations regulate the conduct of members. These provisions are comprehensive and establish and regulate the operations of investigative and disciplinary committees, appeals committees and provide for such matters as hearings, penalties, costs awards and so on.<sup>16</sup> The Investigative, Disciplinary and Appeals Committees may include lay members.

8.13. For example, the ASCPA Articles provide that a member may be penalised where (among other things) he/she has breached the Society's Articles, By-Laws and Pronouncements, engaged in conduct that is dishonourable, derogatory or not in the

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<sup>11</sup> Subsection 1296, Corporations Law.

<sup>12</sup> Sections 1317A–1317D, Corporations Law.

<sup>13</sup> Companies Auditors and Liquidators Disciplinary Board, *Annual Report for the year ended 30 June 1996*, AGPS, Canberra, p. 3.

<sup>14</sup> See citation at note 13.

<sup>15</sup> Companies Auditors and Liquidators Disciplinary Board, *Annual Report for the year ended 30 June 1995*, AGPS, pp. 8–10.

<sup>16</sup> For example, ASCPA Articles 26–32 and By-laws 301.1–310.6 deal with regulation of conduct and disciplinary procedures.

best interests of the Society or its members or has failed to observe proper professional standards, obtained admission by improper means, or has become an insolvent under administration.<sup>17</sup> Penalties that may be imposed include forfeiture of membership, suspension from membership, a fine not exceeding \$50,000, censure and admonishment.<sup>18</sup> In addition, or as an alternative, the member may be required to undertake a course of professional development.<sup>19</sup> The affected practitioner may also be required to pay the costs of investigating and hearing the matter.<sup>20</sup> Appeals are allowed to the National Council where a member would be required to forfeit or suspend membership or pay a fine exceeding \$5,000. However, if the appeal fails, the member is required to pay the costs of the appeal.<sup>21</sup>

8.14. The professional legal bodies in the States and Territories also have disciplinary regimes for their members which are supported by legislation, regulations and rules.

8.15. The IPAA does not have a formal disciplinary procedure. However, if a complaint is made against one of its members, it will investigate the complaint to determine if there is a case for action. If there is such a case, the matter is referred to the appropriate disciplinary committee of the member's foundation organisation, being the accounting bodies or a law society.

## **Commentary**

8.16. Under the current statutory disciplinary system, responsibility for the processes of investigation, hearing and appeal are divided between the ASC, the CALDB and the AAT respectively. Under the system conducted by the professional bodies, various committees of those bodies perform all three roles.

8.17. The main advantage of the current statutory system is independence. The separation of the investigation/hearing/appeal roles between various bodies serves to ensure impartiality and fairness. However, there are considerable disadvantages in terms of costs and delay, particularly in relation to matters which are relatively straight forward, such as the failure to lodge triennial statements.

8.18. There may be considerable savings in costs if the professional bodies could take over the disciplinary role completely. However, a disciplinary system run by the professional bodies could give rise to a perception that the system is not truly independent. In addition, the merging of the investigation/hearing/appeal processes

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<sup>17</sup> Paragraph 27(1) ASCPA Articles.

<sup>18</sup> Paragraph 27(2) ASCPA Articles.

<sup>19</sup> Paragraph 27(3) ASCPA Articles.

<sup>20</sup> Paragraph 27(4) ASCPA Articles.

<sup>21</sup> Paragraphs 30(2), 30(4) ASCPA Articles and By-law 309.

gives rise to obvious concerns about impartiality. Further, it is questionable whether the committees of the professional bodies would be sufficiently funded and equipped to deal effectively with potentially long and complex proceedings.

8.19. Maintaining two parallel disciplinary systems may appear to be unnecessary duplication. However, in relation to matters involving allegations of serious misconduct which could result in substantial penalties, the Working Party considers that there are legitimate concerns in giving the professional bodies responsibility for the disciplinary role. In this regard, consideration should be given to the necessities of having a fair and impartial system and having a system which is seen to be so. The only way of ensuring this would be to have these matters dealt with by an independent body (or bodies).

8.20. It would be possible for the ASC to perform the disciplinary function itself, as it currently does in relation to securities dealers and investment advisers. However, the Working Party considers that, from a fairness perspective, there are advantages in retaining separate responsibility for the investigation and hearing roles, at least in relation to matters involving alleged misconduct.

8.21. The disciplinary procedures in relation to registered liquidators are similar to the procedures in relation to registered company auditors. The Working Party notes that the role of the CALDB and the difficulties mentioned above have been considered in the context of the Review of the Requirements for the Registration and Regulation of Company Auditors.<sup>22</sup> In its draft report, the Working Party conducting that review stated that:

- administrative matters, being the failure to lodge reporting statements or cancellation of registration due to a disqualification or prohibition order, should be dealt with not by a CALDB but by the body charged with registration and general supervision of practitioners (which would, in the case of auditors, be a professional body under authorisation from the ASC);<sup>23</sup>

‘conduct’ matters should continue to be dealt with by the CALDB at a formal hearing and natural justice principles should be observed, unless the ASC agrees to a particular conduct matter being conducted by the registering and supervisory body.<sup>24</sup>

8.22. The Working Party conducting the auditors’ review considered that there is little justification for using the resources of a disciplinary body on matters such as a failure to lodge statements. However, a disciplinary board conducting a formal hearing

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<sup>22</sup> Review of the Requirements for the Registration and Regulation of Auditors, Draft Report prepared by a Working Party appointed by the Commonwealth Government, April 1996, Chapter 9.

<sup>23</sup> See note 22, draft recommendation 9.3.

<sup>24</sup> See note 22, draft recommendations 9.6., 9.7.

and observing the principles of natural justice should be used where matters of judgement and professional knowledge are required, for example, in cases alleging failure to adequately and properly carry out duties and functions.

8.23. A further issue considered by the review dealing with auditors was the penalties that the CALDB was able to impose. Currently, they are permitted to suspend or cancel registration, admonish or reprimand a person. In its draft report, the Working Party dealing with auditors concluded that greater flexibility, particularly in relation to the imposition of fines, would be a desirable reform. In addition, the Working Party recommended that consideration should be given to allowing the CALDB to enforce orders made during the pre-hearing period and use mediation and arbitration.<sup>25</sup>

8.24. The Working Party agrees with the views expressed by the Working Party conducting the auditors review regarding the matters mentioned above. The Working Party considers that there is no reason to distinguish the powers that the CALDB has in relation to those issues in relation to auditors from the powers it has in relation to liquidators.

8.25. The Working Party recommends that the statutory disciplinary procedure involving the ASC, the CALDB and the appeal mechanism to the AAT should be retained for **conduct matters**. However, the professional accounting and legal bodies should also have a right to bring a matter before the CALDB. **Administrative matters** should be dealt with by the registering authority, which is currently the ASC.

8.26. Further, the Working Party recommends that the CALDB should be given greater flexibility in the penalties it may impose and should be given powers to enforce orders made during the pre-hearing period and to use mediation and arbitration.

## REMEDIAL SUPERVISION

8.27. Responsibility for remedial supervision, that is, activities directed at providing a remedy for an inappropriate act or omission by a practitioner in a particular matter, is currently shared by the ASC and the court.

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<sup>25</sup> See note 22, draft recommendation 9.9.

## The ASC

8.28. As discussed earlier in this report,<sup>26</sup> the role of the ASC in relation to remedial supervision encompasses a number of areas.

### Inquiries

8.29. The ASC has power to inquire into the conduct of liquidators, scheme administrators and controllers where complaints are received by the ASC from any person regarding the performance of duties.<sup>27</sup> The ASC may also initiate an inquiry where it appears to the ASC that a practitioner is not faithfully performing his or her duties/functions, or has breached or is not observing a requirement of the Law, the rules or regulations, the court or, in the case of controllers, the order or instrument of appointment.<sup>28</sup>

8.30. Unlike the court, the ASC has not been given specific powers in the Corporations Law to require practitioners to answer questions on oath, or to undertake an investigation into the books of the practitioner.

8.31. The ASC has some compulsive powers which are set out in the ASC Law. The powers of the ASC to inspect books may be exercised for the purpose of the performance of its responsibilities under national scheme laws such as the Corporations Law.<sup>29</sup> Accordingly, in some circumstances, the ASC could use those powers for the purpose of carrying out an inquiry into the conduct of a practitioner. However, generally the powers in the ASC Law regarding compulsory examinations may only be used where the ASC is investigating a possible contravention of the Corporations Law or other statute which concerns the management of a body corporate or involves fraud or dishonesty relating to a body corporate, securities or futures contracts.<sup>30</sup> The powers could not be used in relation to an inquiry into a possible breach of duties or other requirements where there is no ongoing investigation of a contravention of the law.

8.32. Therefore, where a possible breach of duty or other requirements has occurred but there is no formal investigation on foot in relation to a possible contravention of the law, the ASC would need to seek the assistance of the court in order to conduct a compulsory examination.

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<sup>26</sup> See Chapter 3.

<sup>27</sup> Paragraphs 536(1)(b), 411(9)(b), 423(1)(b), Corporations Law.

<sup>28</sup> Paragraphs 536(1)(a), 411(9)(b), 423(1)(a), Corporations Law.

<sup>29</sup> Paragraph 28(a) ASC Law.

<sup>30</sup> Section 13 ASC Law.

8.33. The Working Party is aware that any proposal to expand the ASC's compulsory examination powers is likely to be contentious, particularly in the light of recent criticisms by the Senate Legal and Constitutional References Committee in its report on the investigatory powers of the ASC.<sup>31</sup> However, the Working Party considers that such a proposal should be given consideration because:

- the existence of compulsive powers in relation to inquiries into the conduct of insolvency practitioners can be justified on similar grounds as compulsive powers the ASC already has; and
- the court already has these powers and, arguably, the ASC is a more appropriate body than the court to conduct inquiries into these matters.

8.34. Issues concerning whether, and to what extent, privileges and immunities would apply to an examination, and what rights of review should be available in relation to a decision to exercise the powers, would need to be considered in detail to ensure that an appropriate balance is struck between making the procedure as effective as possible and avoiding practitioners being exposed to an excess of power. However, the Working Party considers that these matters could be resolved by imposing 8.35.

8.35. The purpose of the proposal is not to attempt to maintain appropriate standards of conduct by disciplining practitioners, although disciplinary proceedings might arise out of matters connected with the subject matter of an inquiry. Rather, the proposal would provide an important remedial measure aimed at protecting 'third parties', such as creditors, in particular matters. The outcome of an inquiry could, for example, determine whether the estate of a company should be compensated due to the default of a liquidator.<sup>32</sup> The inquiry may lead to a wider investigation which is not restricted to the conduct of a liquidator, but involves the conduct of directors or other persons and breaches of laws unrelated to liquidator's duties. It is, therefore, important that the inquiries are conducted in a timely manner by a well-resourced body which is completely impartial, and is seen to be so by all concerned.

8.36. The Working Party recommends that the ASC's powers to carry out **inquiries into conduct** should remain. However, consideration should be given to whether the ASC should be permitted to exercise compulsive powers for this purpose, or at least be given an express power to request the court to exercise its own compulsive powers for this purpose. The ASC should also retain its existing powers to submit reports to the court and apply for remedial orders.

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<sup>31</sup> Australia. Parliament, Report by the Senate Legal and Constitutional References Committee, *The Investigatory Powers of the Australian Securities Commission*, June 1995, Canberra, in particular pp. 65—94.

<sup>32</sup> Subsection 536(2), Corporations Law.



## Reports and Applications

8.37. The ASC has power to report any matter to the court which, in its opinion, is a misfeasance, neglect or omission on the part of a practitioner. In response, the court may order the practitioner to make good any loss that the estate of the company has sustained, and any other orders it thinks fit.<sup>33</sup> Like the power to conduct inquiries, this power may be exercised in relation to liquidators, scheme administrators and controllers, but not in relation to voluntary administrators or deed administrators.

8.38. In relation to companies under voluntary administration or a deed of company arrangement, the ASC has the power to apply to the court for orders where the administrator concerned has managed, or is managing, the company's business, property or affairs in a way which is prejudicial to the interests of some or all creditors or members, or where the practitioner has done, or proposes to do, something that would be prejudicial.<sup>34</sup> Creditors and members of the company concerned may also apply to the court in those circumstances,<sup>35</sup> and the court, in response, may make such order as it thinks just.<sup>36</sup>

8.39. There is also a specific power for the ASC or a creditor to apply to the court to seek removal of a voluntary administrator or a deed administrator.<sup>37</sup>

8.40. The ASC has a general power to apply to the court for an order against any person in cases involving fraud, negligence or breach of trust where a corporation has suffered, or may suffer, damage as a result.<sup>38</sup> This application could be made in respect of any practitioner.

8.41. The Working Party considers that these general powers are appropriate and should be retained as they provide a significant degree of flexibility to enable the ASC under the scrutiny of the court to ensure that any person adversely affected by the default of an administrator may be compensated.

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<sup>33</sup> Subsection 536(2), paragraphs 411(9)(b), 423(1)(b), Corporations Law.

<sup>34</sup> Subsection 447E(1), Corporations Law.

<sup>35</sup> Subsection 447E(3), Corporations Law.

<sup>36</sup> Subsection 447E(1), Corporations Law.

<sup>37</sup> Section 449B, Corporations Law.

<sup>38</sup> Subsection 598(2), Corporations Law.

## The Courts

8.42. The role of the courts in relation to the supervision of corporate insolvency practitioners has a long history which is described in Chapter 3. In summary, it encompasses: inquiries into conduct (at the instigation of the ASC or on receipt of complaints); mandatory examinations and inquiries of practitioners; orders for removal; enforcement of duties and supervisory directions; review of remuneration; and making orders for compensation.

8.43. There are essentially two main issues concerning the court's involvement in the process. The first issue is whether it would be more effective for another body to carry out those roles. The second, somewhat related issue, is whether it would be possible for a non-judicial authority to be given responsibility for such matters.

### Inquiries and Examinations

8.44 The court has a general power to conduct inquiries where it appears to the court that a liquidator (including a provisional liquidator) has not faithfully performed his or her duties, or has not observed (or is not observing) a requirement of the court, or the Corporations Law and associated regulations and rules.<sup>39</sup> The court may also conduct an inquiry where a complaint is made to the court by *any person* in respect of the performance by a liquidator of his or her duties.<sup>40</sup> The powers to inquire into the conduct of liquidators also apply to scheme administrators,<sup>41</sup> and there are similar powers relating to controllers.<sup>42</sup> The ASC has identical powers in relation to the conduct of these inquiries. Where the ASC or the court carries out such an inquiry, the court may take 'such action as it thinks fit'.<sup>43</sup> No guidelines as to the conduct of the inquiries are set out in the Law or in the associated regulations, although the rules of the courts contain some provisions which address some procedural aspects.<sup>44</sup> For the most part, the procedure to be followed is determined by the court in each particular case, having regard to the interests of fairness.<sup>45</sup> Inquiries by the court are not automatic on receipt of a complaint—the court must be satisfied that it is in the public interest to conduct an inquiry.<sup>46</sup> The ambit of the inquiry is for the court to determine and may include other administrations in which the practitioner has been involved.

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<sup>39</sup> Paragraph 536(a), Corporations Law.

<sup>40</sup> Paragraph 536(b), Corporations Law.

<sup>41</sup> Paragraph 411(9)(b), Corporations Law.

<sup>42</sup> Subsection 423(1), Corporations Law.

<sup>43</sup> Subsection 536(1), Corporations Law.

<sup>44</sup> See for example Order 71 Rule 73 of the Federal Court Rules, Part 80A Rule 29 of the NSW Supreme Court Rules.

<sup>45</sup> *CCA v Harvey* [1979] ACLC 32,296 at 32, 317.

<sup>46</sup> *Burns Philp Investments Pty Ltd v Dickens (No 2)* 10 ACSR 626.

8.45. It is arguable that courts are not generally geared to conducting these inquiries. This issue was discussed in detail by Marks J in *CCA v Harvey*.<sup>47</sup> However, it has also been noted by courts on some occasions that, despite the use of the word ‘inquiry’ in the legislation, inquiries by the court into conduct of practitioners are essentially adversarial proceedings between the practitioner and the party making the complaint.<sup>48</sup> In practice, the complainant will set out, by way of affidavit, the grounds on which the inquiry is sought and possibly also the nature of the relief sought. Commonly, this will include substantive orders such as the removal of the practitioner from the administration, requiring a practitioner to pay compensation, or ruling on entitlements to remuneration and expenses. In addition to substantive orders, the court may make ‘findings’ about the conduct which may be of considerable significance to the practitioner concerned.<sup>49</sup>

8.46. The Working Party considers that, except in the case of administrators appointed by the court, who are the court’s own officers, there are no readily apparent reasons for the courts to retain powers to undertake inquiries of their own motion. Except in the case of official liquidators, the court’s role in supervision should be limited to determining matters brought before it by the parties and, where appropriate, making orders in that regard. Although, in practice, this is essentially how the provisions have operated, it may be desirable to clarify the position on the face of the legislation.

8.47. In some cases, the ASC will not be in a position to fund an investigation or court proceedings within the time frame sought by the complainant or at all. The Working Party, therefore, considers that it should be possible for a person to seek the direct intervention of the court in particular cases of alleged breach of duty, legislation or court requirements. However, the court should not be responsible for ‘inquiring’ into complaints in the sense of gathering evidence, examining books and so on.

8.48. The Working Party notes that certain aspects of the role of the court in supervising practitioners are currently subject to challenge in the High Court.<sup>50</sup> Regardless of the outcome of that litigation, the Working Party considers that there would be advantages in reviewing the role of the courts in supervising insolvency practitioners in order to ensure that the system works effectively. For this purpose, consideration should be given to the matters mentioned above.

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<sup>47</sup> [1979] ACLC 32,296 at 32, 317; (1979) 4 ACLR 259 at 275.

<sup>48</sup> See, for example, *Re Day & Dent Constructions Pty Ltd (in liq)* ((1985) 3 ACLC 98 at 113.

<sup>49</sup> *Re Ah Toy* (1986) 4 ACLC 480 at 483.

<sup>50</sup> *Gould v Brown (In his capacity of Amann Aviation Pty Ltd)*—Matter No 125 of 1996. Appeal to the High Court from the judgement and orders of the Federal Court given and made on 24 June 1996 in the matter of *BP Australia v Amann Aviation Pty Ltd* (1996) 21 ACSR 108.

8.49. The Working Party recommends that the provisions of the Corporations Law concerning the role of the court in supervising practitioners should be reviewed.