

**ASIC**

Australian Securities & Investments Commission

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14 – 22 Grey Street, Traralgon  
PO Box 4000  
Gippsland Mail Centre VIC 3841

Facsimile: (03) 5177 3999  
ASIC Homepage: [www.asic.gov.au](http://www.asic.gov.au)



Dear Registered Liquidator,

**Independence Project - review of compliance by registered liquidators with the new disclosure requirements**

For voluntary administrations and creditors' voluntary windings-up that commenced on or after 31 December 2007, registered liquidators are required to provide to creditors, with the notice of the first meeting of creditors, Declarations of relevant relationships and indemnities<sup>1</sup>.

The Explanatory Memorandum to the Corporations Amendment (Insolvency) Act 2007 ("Explanatory Memorandum") explained that the new disclosure laws were introduced to assist creditors to consider, at an early stage of an appointment, whether the registered liquidator is sufficiently independent. A key theme of the reforms was that creditors are to be provided with information to alert them to relationships that, although they may not give rise to a conflict, may be relevant to creditors in considering and making an informed decision about the independence of the registered liquidator and whether to replace the registered liquidator<sup>2</sup>.

**Independence Project findings**

During 2009 ASIC undertook a project to assess compliance by registered liquidators with the new disclosure requirements relating to relevant relationships and indemnities.

ASIC reviewed 239 Declarations (involving external administrators from 79 firms) against:

- statutory requirements; and
- industry guidance provided in the Code of Professional Practice published by the Insolvency Practitioners Association of Australia ("IPA").

The review identified a number of areas where we believe the adequacy of disclosure needs improvement. In particular, our general observations are that:

- a large number of Declarations did not adequately disclose the nature of the relationships or provide adequate reasons to explain why the disclosed relationships did not result in a conflict of interest or duty;
- Declarations did not clearly articulate whether the registered liquidator's firm (i.e. partners or related bodies corporate) was included in the Declaration;

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<sup>1</sup> The relevant sections of the Corporations Act 2001 are sections 9, 11, 60, 436DA and 506A

<sup>2</sup> Explanatory Memorandum to the Corporations Amendment (Insolvency) Act 2007 paragraphs 4.71 - 4.82

- the majority of Declarations did not disclose the nature and extent of pre-appointment meetings and advice;
- prior or contemporaneous appointments as external administrators of other companies with common directors were not adequately disclosed in over 20 instances;
- many Declarations did not provide sufficient information to adequately identify the party providing an indemnity or sufficiently disclose the nature and extent of the indemnity provided;
- many Declarations were not signed by both joint and several appointees (ASIC is of the view that each appointee must consider whether any relevant relationships exist that require disclosure and the Corporations Act 2001 ("the Act") requires each appointee to sign the relevant Declarations); and
- it was not evident from the minutes of the meeting of creditors in many cases that Declarations were tabled at the meeting of creditors as required by the Act<sup>3</sup>. Minutes of the meeting of creditors should evidence compliance with this statutory requirement.

### **Required disclosure**

Registered liquidators must comply with the disclosure requirements in the Act.

ASIC expects that registered liquidators will disclose sufficient information about all relevant relationships and indemnities to enable creditors to make an informed decision about whether to replace the voluntary administrator or liquidator in a creditors' voluntary winding-up at the first meeting of creditors<sup>4</sup>.

#### *Relationships that require disclosure*

ASIC considers that the types of relationships that might be relevant and material to creditors when considering and making an informed assessment of the registered liquidator's independence include:

- pre-appointment meetings with the company, its accountant or other advisor;
- other external administrations with common directors where the registered liquidator or someone in their firm is, or has been in the preceding 24 months, the appointed external administrator;
- prior personal or professional relationships that the registered liquidator or their firm has, or has had in the preceding 24 months, with the company or an associate of the company; and
- prior appointment as an investigating accountant of the company.

In deciding whether to disclose any particular relationship the registered liquidator should consider whether a creditor might consider knowledge of that relationship as a relevant factor in their assessment of the independence of the registered liquidator - regardless of whether or not the registered liquidator considers that the relationship would or may be perceived to give rise to an actual or potential conflict.

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<sup>3</sup> Refer sections 436DA(4) and 506A(4)

<sup>4</sup> Explanatory Memorandum to the Corporations Amendment (Insolvency) Act 2007 paragraph 4.71

The type of information that would assist creditors in understanding the nature of the relationship and its potential impact on the registered liquidator's ability to act independently includes:

- the name of the party with whom the relationship exists (rather than simply stating there is a relationship with, for example, 'major banks');
- the nature of the relationship; including the nature and scope of any work done or advice given to the company (or an associate of the company), the frequency of contact, fees received in respect of the work etc;
- the period of time over which the relationship has existed; and
- where the relationship is with a secured creditor – the significance of that relationship to the firm.

Registered liquidators should provide sufficient information about the nature of relationships to assist creditors in forming their own view about the independence of the registered liquidator.

#### *What is an adequate reason*

A Declaration of Relevant Relationships must state the registered liquidator's reason for believing why none of the relationships disclosed result in them having a conflict of interest or duty<sup>5</sup>.

We understand that it may be difficult to articulate why a particular relationship does not result in a conflict of interest or duty. However, we do not believe the following statements provide an adequate reason:

#### **a. Disclosure of relationships with secured creditors**

- "the relationship has not impeded our independence";
- "the relationship is generally governed by regulations and is conducted on a professional basis";
- "it is a commercial relationship"; or
- "we will be acting in the interests of creditors and professional relationships in other unrelated matters won't affect our independence in this matter."

#### **b. Disclosure relating to pre-appointment meetings or advice**

- "the advice will not influence our ability to comply with the statutory and fiduciary obligations associated with the appointment"; or
- "the pre-appointment work was not paid for".

#### **c. Disclosure relating to other professional services**

- "it does not relate to the day to day operations of the company" (where personal taxation services are provided to the directors); or
- "immaterial fee amount" (where taxation services were provided to the company).

#### **d. Disclosure relating to acting as external administrator of related companies with common directors**

- "the appointments will not affect the independence of the external administrators in fulfilling their role in the administration of the company and the acceptance of the appointment is not in contravention of the relevant legislation".

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<sup>5</sup> Refer section 60

The statements are not adequate because they do not state why the relationship (including the work performed or advice given) will not impede or inhibit the registered liquidator's ability to act independently, impartially and in the interests of creditors.

#### *How indemnifying parties should be identified*

A Declaration of Indemnities must disclose the identity of the indemnifying party<sup>6</sup>.

ASIC expects that the Declaration should name the indemnifying party. It is not sufficient to disclose that an indemnity has been received from a Director or Shareholder in circumstances where there is more than one party who could potentially be the indemnifying party.

#### *What information about indemnities should be disclosed*

A Declaration of Indemnities must disclose the nature and extent of any indemnity provided<sup>7</sup>.

ASIC expects that the Declaration will provide sufficient details about what the indemnity covers (i.e. whether it covers remuneration and/or expenses and/or other debts or liabilities) as well as any conditions or monetary limit or cap that is placed on the indemnity.

#### *How inquiries should be documented*

The Act provides a defence against prosecution for an inadequate Declaration where, based on reasonable inquiries, a registered liquidator has reasonable grounds to believe that a matter need not be disclosed in the relevant Declaration<sup>8</sup>.

ASIC expects that registered liquidators will have processes and procedures in place to adequately document all the inquiries made prior to completing the required Declarations. This would include checklists that are completed to document any searches or inquiries that they undertake.

### **What you should do**

You should:

- review your policies and procedures to ensure that you are able to adequately identify and investigate all relevant relationships that require disclosure;
- ensure that you adequately disclose all relevant relationships and indemnities in future Declarations; and
- assess your needs and undertake training, as required, to ensure compliance with the requirements of the Act.

### **Ongoing liaison with the IPA**

As well as monitoring ongoing compliance by registered liquidators with their disclosure requirements, ASIC is liaising with the IPA to enhance the guidance provided in its Code of Professional Practice about additional relationships and information that, if disclosed, might be relevant to a creditor when assessing the independence of a registered liquidator.

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<sup>6</sup> Refer section 9

<sup>7</sup> Refer section 9

<sup>8</sup> Refer s436DA(7) and 506A(7)

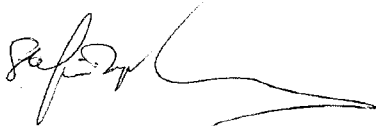
Issues being discussed include:

- disclosing further information to allow creditors to assess the significance of the relationship with a secured creditor in an external administration appointment to the registered liquidator and their firm;
- disclosing the relationship, if any, between the registered liquidator, or their firm, and the party who referred the external administration appointment;
- disclosing whether a significant creditor in an external administration appointment is, or has been, a client of the registered liquidator or their firm in the preceding 24 months; and
- providing guidance to assist registered liquidators in stating adequate reasons for believing why none of the relationships disclosed result in them having a conflict of interest or duty.

Following these discussions, ASIC may issue a consultation paper and draft regulatory guide seeking broader comment on the independence of registered liquidators and the disclosure of relevant relationships and indemnities.

If you have any questions about the outcomes of the review please contact me by email at [stefan.dopking@asic.gov.au](mailto:stefan.dopking@asic.gov.au).

Yours faithfully



Stefan Dopking  
Senior Executive Leader  
Insolvency Practitioners & Liquidators Stakeholder Team