ARITA
AUSTRALIAN RESTRUCTURING INSOLVENCY & TURNAROUND ASSOCIATION

23 September 2016

Financial Ombudsman Service Australia
By email: smallbusiness@fos.org.au

Dear Sir/Madam

## Expansion of FOS's Small Business Jurisdiction – consultation paper

Thank you for the opportunity to lodge a submission on the consultation paper 'Expansion of FOS's Small Business Jurisdiction' (Consultation Paper). Our submission refers to only some of the consultation questions, primarily relating to the proposal to ensure that relevant third parties attend FOS 'small business credit facility' (SBCF) dispute resolution conferences.

## Key points

ARITA submits that Proposal 1.2 to compel 'relevant third parties', such as insolvency practitioners, to be joined to or participate in the FOS dispute resolution process is analogous to the grant or introduction of a power of subpoena. We believe such a power should properly remain in the jurisdiction of the courts, where subpoenas are necessary for the administration of justice and can be supervised by judicial officers in order to guard against potential abuse of process or oppression.

An effective power of subpoena (or its equivalent) is not appropriate for an external dispute resolution scheme. In any event, the proposal would appear to serve little purpose when a FOS process cannot impose any outcome or remedial order against a non-party to a dispute.

Compelling insolvency practitioners to attend or participate in a dispute resolution process would also impose an unreasonable cost burden on the administration of insolvent small business debtors – a cost which ultimately will be borne by creditors through reduced returns and distributions.

Yours sincerely

**John Winter**
Chief Executive Officer

# About ARITA

The Australian Restructuring Insolvency and Turnaround Association (ARITA) represents practitioners and other associated professionals in Australia who specialise in the fields of restructuring, insolvency and turnaround.

We have more than 2,200 members including accountants, lawyers, bankers, academics and other related professionals.

ARITA's mission is to support restructuring, insolvency and turnaround professionals in their quest to restore the economic value of underperforming businesses and to assist financially challenged individuals.

We deliver this through the provision of innovative training and education, upholding world class ethical and professional standards, partnering with government, and promoting the work of the profession to the public at large.

Some 84 percent of registered liquidators and 89 percent of registered trustees choose to be ARITA Professional Members.

ARITA promotes best practice and provides a forum for debate on key issues facing the profession. We engage in thought leadership and advocacy underpinned by our members' knowledge and experience.

# Proposal 1.2: Compelling the attendance or participation of a relevant third party

## Consultation Questions for Proposals 1.1 to 1.3

***Do you agree with FOS expanding its small business jurisdiction and Proposals 1.1 to 1.3? If not, why not?***

***How would the proposals affect your organisation or constituents? Wherever possible could you quantify any costs or benefits anticipated and include examples?***

***Can you provide other information about the effect of the proposals?***

Proposal 1.2 of the Consultation Paper is to '[p]rovide for paragraph 7.3 [of the FOS Terms of Reference] to apply to SBCF disputes in a way that allows FOS, when considering such a dispute, to require a party to [i] attend a compulsory conference and [ii] ensure that a relevant third party also attends the conference.'

Insolvency practitioners of a small business borrower or guarantor are specifically mentioned as one category of third party which, at present, FOS cannot compel to participate in its dispute resolution process. The Consultation Paper also seeks 'any suggestions or feedback about approaches' which could be taken 'to address the limitation on FOS's ability to compel relevant third parties to be joined to or participate in the dispute resolution process.'

At the outset we note that the Consultation Paper is silent as to how the apparent desired outcome of legal compulsion would be implemented or achieved. As reflected in the terms of the Consultation Paper quoted above, it is not entirely clear if the proposal is intended to impose a requirement *on parties* to ensure the participation of a relevant third party, or whether it is being suggested that FOS might be invested with a power to do so.

Either way, we are not sure how third parties (non-parties) could be compelled to attend a FOS process in the absence of enabling legislation which would grant such a power to require attendance.

### Equivalent power of subpoena is inappropriate for FOS's external dispute resolution scheme

Any power of FOS (or the parties to a dispute) to compel 'relevant third parties', such as insolvency practitioners, to be joined to or participate in a FOS dispute resolution process would be analogous to a power of subpoena. A subpoena is the power of a court, on its own motion or at the request of a party, to require a person to attend court to give evidence, produce documents or both.

While subpoenas have been described as a necessary power to enable a court to effectively 'carry on the administration of justice', their exceptional nature has been acknowledged as

an 'invasion of the rights of a stranger' to a dispute.[1] Importantly, court rules and judicial oversight guard against the potential misuse or abuse of subpoenas. For example, courts may hear objections to – and set aside – subpoenas on the grounds of want of relevance, extraneous/ulterior purpose or oppression.

For these reasons, a power of subpoena (or its equivalent) should properly remain in the jurisdiction of the courts and is not an appropriate power for an external dispute resolution scheme.

In any event, the proposal to compel the attendance of a 'relevant third party' would appear to serve little purpose given that a FOS dispute resolution process cannot impose any outcome or remedial order against a non-party to a dispute. This reality is already reflected in the FOS's own Fact Sheet which details how disputes are handled if the applicant is insolvent.[2]

### Cost to insolvency practitioners of compulsory attendance

Compelling insolvency practitioners to attend or participate in a dispute resolution process would also impose an inevitable cost burden on insolvency practitioners. As with all necessary and proper costs associated with the insolvency practitioner's conduct of an insolvency administration, these will be met out of what (often little) assets remain for the benefit of a distribution (dividend) to creditors.

The costs of insolvency practitioners' compulsory attendance at FOS dispute resolution conferences will become another expense of the external administrations or bankruptcies of small business borrowers, which ultimately will be borne by creditors through reduced returns.

If the FOS process were to take place after the completion of an administration, that insolvency practitioner may be left in a situation where the costs of their involvement in a FOS process, including forgone billable hours, would not be recoverable from the completed administration, leaving the insolvency practitioner without any recourse for costs.

### Potential conflict with the customary role and duties of insolvency practitioners

Any new power to compel insolvency practitioners to attend or participate in a FOS dispute resolution process would also be at odds with the independent role and duty of an insolvency practitioner upon his or her appointment to an insolvent business.

Insolvency practitioners appointed to a small business borrower administer and implement an insolvency law regime for the benefit and the interests of a variety of stakeholders. In liquidations and administrations, the primary stakeholders are all creditors as a whole while

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[1] *Summers v Moseley* (1834) 2 C & M 477; 149 ER 849; *Re BLBS and Minister for Foreign Affairs and Trade* (2012) 129 ALD 380 at 392 [32].
[2] FOS Fact Sheet 'How we handle disputes involving insolvent individuals and small business' available at https://www.fos.org.au/small-business/fact-sheets/.

in a receivership it is usually a secured creditor which has enforced its security interest by appointing a receiver.

The broad powers conferred on insolvency practitioners upon their appointment are exercised subject to strict fiduciary and statutory duties owed by the insolvency practitioner. Liquidators and administrators must generally exercise their powers in the interests of creditors as a whole. Receivers exercise their powers in the interests of their appointor (secured creditor), while still owing the company equitable and statutory duties of good faith and reasonable care and diligence.

That all said, creditor stakeholders (or any committee of inspection comprising select creditors) cannot 'direct' how an insolvency practitioner performs his or her functions or exercises his or her powers.

We are also concerned for the implications of any new power on the part of FOS which might potentially compel the production of books from an external administrator or trustee-in-bankruptcy. (Theoretically that would include the Official Trustee in Bankruptcy, the Inspector-General of the Australian Financial Security Authority, meaning that FOS would be seeking the power to compel the participation of a government agency.)

Relevant legislation presently provides for restricted rights of access to the books which an insolvency practitioner is required to keep in the course of the conduct of an appointment. For example, s 531 of the *Corporations Act 2001* (Cth) and Regs 5.6.01 and 5.6.02 of the *Corporations Regulations 2001* (Cth) provide for the ability of a creditor (or contributory) to inspect books which a liquidator must keep in order to give a complete and accurate record of the liquidator's administration of the company's affairs. This right afforded to creditors reflects their usual primacy as a stakeholder in an insolvent liquidation.

## Participation by insolvency practitioners in FOS dispute resolution processes should remain voluntary

Of course, insolvency practitioners can and will continue to consider – on a case-by-case basis – requests by FOS for the practitioner's involvement in any dispute resolution process, in accordance with current practices reflected in the FOS Fact Sheet referred to above.[3]

Insolvency practitioners will assess such requests in the context of their broader role and duties referred to above. As FOS alludes to in its Fact Sheet, if an insolvency practitioner is not prepared to agree to such involvement, and another party is of the view that such involvement is necessary, then a court is the appropriate forum for the matter to be resolved (including potentially by subpoena).

[3] Ibid.