Submissions on the Review of Corporate Insolvency Law

Report No. 2 of the Insolvency Working Group, on voidable transactions, Ponzi schemes and other corporate insolvency matters

23 June 2017

Ernst & Young

Questions for submitters on Report No. 2 When responding to the questions below please include your reasons and supporting evidence.	
Chapter 1: Voidable Transactions	
1	(a) Do you agree with the Insolvency Working Group's assessment of the impact of the Supreme Court's decision in *Allied Concrete v Meltzer* on New Zealand's voidable transactions regime? (paragraphs 32-34) *Yes* (b) If not, what is your assessment of the impact of the decision? *Not Applicable*
2	(a) Do you agree with the Insolvency Working Group's listed objectives of the voidable transactions regime? (paragraph 53) *Yes* (b) Should other objectives also be considered? *We don't believe that any other objectives need to be considered.* (c) What weighting should be given to the objectives, e.g. equally or differently? *We believe the objectives are all important however objective A, the principle of pari passu, should be of primary importance, then B and then C. Pari passu is a long standing objective of insolvency regimes to assist those creditors who did not have an opportunity to enhance their chances of payment prior to a company failure and so to ensure fairness and even-handedness. Two examples of why creditors do not have equal rights in the period leading up to an insolvency event, we are currently dealing with a liquidation where it is apparent that certain creditors were preferred on the basis of which Bank they were a customer of or whether they held debtor insurance or not. Debtor insurance policies are generally not valid if debtors go beyond 60 days and therefore the supplier must cease to trade with them to maintain their insurance cover.*
3	(a) Do you agree with the Insolvency Working Group's views on the problems with the status quo? (paragraphs 56-69) *We agree with the Working Group's views* (b) Are there other problems? *We think we should align with Australia and utilise the peak indebtedness test within the specified period. For example, if someone only started trading with a company 15 months prior to the liquidation, their start point will be zero and therefore no payments they receive can be voidable even if they get fully paid in preference to any other creditor. If the clawback period is reduced to 6 months, the peak indebtedness test is not necessary.*
4	(a) What are your views on the package of changes recommended by the Insolvency Working Group in Chapter 1? (recommendations 1 and 2 and paragraphs 72-77)

	We haven't formed a firm view on whether the time should be 6 months or 12 months but we do note that many Court appointment liquidation companies have ceased trading more than 6 months prior to the commencement date. Creditors who have received partial payment may delay liquidation proceedings to put their payments outside a 6 month period. (b) Do you agree with the Insolvency Working Group that recommendations 1 and 2 need to be implemented as a package? (paragraph 70) If possible, please provide information on the number of voidable transactions that you are aware of that fall within the *specified period* (but not the restricted period) and the dollar amount of such claims. *We agree that the recommendations should be implemented as a package.*
5	Are there other feasible options? *Nothing further to add at this time*
Chapter 2: Other issues relating to voidable transactions and other recoveries	
6	(a) What are your views on the other changes to the voidable transaction regime and other recoveries recommended by the Insolvency Working Group in Chapter 2? (recommendations 3-11) *We agree with the recommendations.* *R9 – What would the test be to show there was no preference, how do they evidence that? For example, how can someone with stock or inventory security show they were paid from the realisation of their secured items or that the secured items were on hand at the time of the payment being made, particularly after the fact with a company in liquidation that in all likelihood did not keep good records?* (b) Are the recommendations likely to have a material impact on the total amount of funds that liquidators would be able to recover under the voidable transaction for the benefit of creditors and, if so, how? *Yes we believe that the recommendations will have a likely impact on the funds recovered. The recommendations will clarify the law and therefore encourage more settlements. There will be a lesser need for court proceedings and therefore Liquidators costs will reduce, allowing more funds to be distributed.* (c) Do you agree that the limitation period for voidable transaction clawback claims should be reduced from 6 to 3 years? (recommendation 7) How often are voidable transaction claims initiated 3 years after the commencement date of the liquidation? *Yes we agree that the limitation period time should be reduced as 3 years is more than sufficient*
7	Do you agree with the Insolvency Working Group's view that the recommendations contained in Chapter 2 can be made with or without making the changes recommended in Chapter 1? *Yes we agree they can be made without making the changes recommended*

	in chapter 1.
Chapter 3: Procedural issues	
8	(a) What are your views on the procedural changes proposed by the Insolvency Working Group in Chapter 3? (recommendations 12-15) *We agree they are sensible and logical proposals.* (b) In regard to recommendation 13 (content of liquidator's notice to set aside transactions) what standard and basic (**additional**) information should a liquidator's notice to creditors under section 294 provide and why? How would the creditor receiving the notice benefit from receiving this additional information and what would be the costs to the liquidator in providing the information? *We agree with what is proposed*
Chapters 1-3: Voidable transactions and recoveries generally .	
9	Are there any other issues with the voidable transaction and other recoveries regime that are not covered by Chapters 1 to 3 of the Insolvency Working Group's report? *We are of the opinion that the Liquidator's burden of proof in relation to transactions with related parties should be minimised ie Liquidator should only have to prove insolvency existed but not have to prove related party's knowledge of insolvency.*
Chapter 4: Ponzi schemes	
10	What are your views on the possible changes to the Property Law Act 2007 outlined by the Insolvency Working Group to aid the recovery of funds (adding a Ponzi presumption and a good faith defence)? (recommendation 16(a)) *We have no comment.*
Chapter 5: Other corporate insolvency issues	
11	(a) What are your views on the other corporate insolvency law changes proposed by the Insolvency Working Group in Chapter 5? (recommendations 17-30) *We agree with recommendations 17-30 except for recommendation 25 regarding gift cards as detailed below.* (b) What are your views on allowing liquidators to obtain, by right, certain information from third parties without having to go to the High Court? (recommendation 20 and page 48) What are the costs involved in seeking an order from the High Court? Does the High Court routinely approve such requests? *We agree with this recommendation as long as it specifies that information is*

	related to the business or dealings of the company *Costs involved include legal, filing and administrative costs* *Yes the High Court does approve these requested that we have been involved with* (c) Do you agree that it is not clear whether long service leave forms part of Schedule 7 of the Companies Act? (recommendation 24 and page 51) How often does the possible recognition of long service leave as a preferential claim arise? *Yes we agree that clarity is needed to provide certainty to liquidators, employers and employees. We do not see the situation arise arising regularly, however, believe it warrants updated schedule 7 to provide certainty to all relevant parties and ensure a consistent approach is taken by Liquidators.* (d) What are your views on establishing a new preferential claim for gift cards and vouchers? (recommendation 25 and pages 51-52) *We disagree with this recommendation. This would significantly increase the administration costs in receiverships, voluntary administrations and liquidations having to deal with these claims in priority to other preferential and unsecured creditors and therefore reduce payouts overall to all creditors.* *We believe there would be better mechanisms to provide consumer protection than a creating a preferential claim such as requirement for the establishment of a trust for gift cards and vouchers whereby these funds would need to be held on trust until they are spent. We believe larger entities or third parties on behalf of smaller entities could administer these trusts in a cost effective manner.* (e) What are your views on the recommendation to limit the preference claims of the Commissioner of Inland Revenue and the Collector of Customs to six months prior to the date of the commencement of the liquidation? (recommendation 26 and pages 52-53) *We agree that the IRD and Customs preferential claim periods should be limited. This will possibly see the Commissioner act earlier on a defaulter than is currently the case. Thus enabling better recovery of assets for all creditors. At the same time, it should be made easier for the Commissioner to take action against directors who do not comply with their IRD requirements and penalties should be increased as a deterrent.* (f) What aggregate information, if any, would be useful for the Registrar of Companies to publish and why would it be useful? (recommendation 30 and page 56) *We believe that information and statistics relating to the number of appointments, the process (receivership, liquidation voluntary administration), industry of the company (using ANZIC industry codes that new companies have to provide when registering) and the length of the assignment are the obvious statistics to provide. However, we also believe that providing the quantum of creditors who have claimed in the liquidation by class, the number of creditors by class and distributions made to creditors would provide*

	invaluable information for academics, officials and other parties to assess the efficiency of the corporate insolvency system and effect insolvency has on the wider community
12	(a) What are your views about the Insolvency Working Group's comments on the corporate restructuring processes in New Zealand? (paragraphs 173-177)[1] *We agree with the comments of the Working Group in regards the corporate restructuring processes in New Zealand.* (b) Does New Zealand's insolvency regime meet the OECD's objectives outlined in paragraph 173? *We believe that New Zealand does meet the OECD's objectives* (c) How important is it for New Zealand's insolvency regime to be aligned with the Australian regime? *We believe alignment should be a goal, however, deviation allowed where circumstances justify.*
13	Are there any other changes to corporate insolvency law not covered in Report No. 2 that should be made? ***Section 280 of the Companies Act*** *Yes, we have some comments regarding s280(1)(cb) – we believe the wording is ambiguous and it should be made clearer that the section includes relationships with any people who have held the position of director but who have resigned within the previous 2 years and a person/entity who was the majority shareholder within the previous 2 years but who has disposed of their shareholding. We also think that secured creditors should only relate to related parties who are secured creditors* ***An unperfected security interest should be an unsecured creditor.*** *More and more we are seeing extremely broad terms of trade entered into between companies and their suppliers, in particular in relation to inventory and goods provided. The terms include the standard security interest over the goods provide and the proceeds thereof but also go significantly further and incorporate the terms of an Auckland District Law Society General Security Agreement by reference and a mortgage over any interest in any property (land) owned by the Company or the guarantor. We believe the addition of the GSA and the mortgage security makes these agreements oppressive but a yet to be tested by the Courts. What this means in relation to a liquidation as where you have made a recovery and perfected purchase money security interest holders, perfected security interest holders and out preferential creditors in full before you can pay out unsecured creditors you need to pay out unperfected security interest holders. We believe change the relevant sections of the Personal Property Securities Act and schedule 7 of the Companeis Act would provide the following benefits:* • *Align with the pari passu principle – The reason these suppliers are unperfected is that because if they perfected their security interest then GSA holders (primarily Banks) would need to enter into a priority agreement with*

[1] Report No. 2 was finalised before 28 March 2017, which was the date that the Australian Minister for Revenue and Financial Services, the Hon Kelly O'Dwyer, released the draft Treasury Laws Amendment (2017 Enterprises Incentives No. 2) Bill 2017 for public comment. The draft Bill, along with the accompanying documents, details the safe harbour and *ipso facto* clause changes discussed in paragraph 176 of Report No. 2. Submissions closed on 24 April 2017.

	them to ensure they have a first ranking security which would become administratively quite burdensome if they had to do this across a wide range of customers. Their intended security in these situations is generally for the goods they have supplied and the proceeds thereon for which they can receive a purchase money security interest (highest priority). To gain an additional priority over unsecured creditors due to clever legal drafting we believe goes totally against the pari passu principle in that the same class of creditors should be treated equally.r • *Reduce cost of administration – Reviewing all the different terms of trade to see the extent of their securities when they did not have a perfected interest is time consuming and there can be a significant number especially where you are dealing with construction related suppliers* • *Align with Australia – In Australia unperfected security interest holders are unsecured* ***Directors should be required to file a statement of affairs for the Company in a liquidation or automatically be banned*** *More and more, especially in court liquidations, we are seeing directors absolve themselves or all responsibility and not even communicate with liquidators. While Liquidators have powers to compel a director to provide information these powers are worthless if there are no funds in the liquidation and you have not being able to identify any company assets to realise as funds are generally required to undertake enforcement action to get a director to comply. In a bankruptcy, the 3 year period before a bankrupt can be discharged does not commence until the bankrupt files their statement of affairs. We believe a similar approach should be taken in liquidations whereby if directors failed to file a statement of affairs on the company in liquidation and provide the company records within a set period to the liquidator then that director should be automatically banned by the Registrar of Companies from being a director of a company on notification from the Liquidator. The automatic ban could later be lifted if the Director subsequently complied. We note the Registrar of Companies should not be required to personally serve the banning order on the director as there would be a significant cost to this if the director did not want to be located but could be done through service by email, address listed at the Companies Office and/or by public advertisement.*
Chapter 6: Implications for personal insolvency law	
14	Do you agree that if recommendations 1-13, 15, 17 and 24-27 were implemented, that these changes should also be made to the Insolvency Act 2006? *Yes we agree that the above recommendations should also be made to the Insolvency Act 2006*
Other comments	
15	Do you have any other comments on Report No.2? *No*

Submission response form

Consultation on whether to introduce a director identification number

Please send your submission to **corporate.law@mbie.govt.nz** by **23 June 2017.**

Please provide your contact details below with your submission.

Name

Organisation **Ernst & Young**

Email address or physical address

Are you providing this submission:

☐As an individual

☒On behalf of an organisation

Large professional services organisation

Please select if your submission contains confidential information:

☐I would like my submission (or specified parts of my submission) to be kept confidential, and attach my reasons for this for consideration by MBIE.

Reason:

1 Are you aware of the issues identified? Please describe the extent to which you think they are a problem.

We are aware of the issues identified and believe it is a significant issue. As Liquidators of companies we regularly see names spelt/stated differently across different companies they may be appointed to and different addresses listed. Being able to quickly and accurately identify a particular director is essential. At the moment, as discussed in the consultation document, it is easy for a person to misrepresent themselves, whether purposely or accidentally, simply by recording their name in a different manner, eg James Smith and Jim Smith. An identity number as described would remove that possibility and provide the public with assurance that they have identified the correct person and all of his/her directorships.

2 Are there any other issues that we have not identified? If so, please describe them and provide evidence if available.

Yes, we have identified a few other issues/considerations. These are as follows:

a) Would there be a prescribed time period, by which if a person has been inactive as a director that their number is deactivated and would this be publically available?

b) Our legislation contains a requirement that every company must have at least one director that lives in New Zealand or lives in Australia and is a director of a company incorporated in Australia[1]. We note that the Australian government has now responded to the Australian Productivity Commission's report which you mentioned at paragraphs 16 and 17 of your Discussion Paper and has stated that it will consider introducing the director identification number requirement in Australia. [2] Assuming this goes ahead, would Australian directors be able to use their Australian director identification number or would they be assigned a new number on becoming a director of a New Zealand company? In either case, would the New Zealand Companies Office be able to rely on the information collected by its Australian counterpart, the Australian Securities & Investments Commission, and thereby simplify the registration requirements for Australian directors of New Zealand companies who already have Australian director identification numbers?

c) The New Zealand Companies Office maintains a number of registers of various other bodies, not just companies. Is there a proposal to introduce similar requirements in relation to office holders of these other bodies as, arguably, the same or similar issues arise in respect of these bodies? Would it not be sensible to introduce the requirement under the definition of an 'officer identification number' so that it can be of universal application regardless of what the body in question is? For instance, many bodies corporate working in the not-for-profit sector chose to incorporate themselves under the Incorporated Societies Act 1908, which is currently subject to reform[3]. We note that much of the proposed Incorporated Societies Bill has been modelled on the Companies Act 1993 so it would make sense for the 'director/officer' identification number requirement to be introduced in the Incorporated Societies Bill too.

3 Do you think a director identification number is the best way to address the issues identified?

Yes. As with other agencies (IRD, ACC, WINZ, NHI), an identification number would allow speedy, efficient and accurate processing. Furthermore, it would allow a registered director to easily become a director of a new company without requiring the usual forms to be completed and uploaded. A director could potentially enter their number and click to confirm they are not disqualified. Most importantly it will provide a greater level of

[1] Section 10(d) of the Companies Act 1993 and Regulation 12 of the Companies Act 1993 Regulations 1994

[2] Please see the Australian Government response to the Productivity Commission Inquiry into business set-up, transfer and closure, May 2017, page 30 (Government response to recommendation 15.6): http://treasury.gov.au/~/media/Treasury/Publications%20and%20Media/Publications/2016/Government%20response%20to%20the%20Productivity%20Commission%20Inquiry%20into%20Business%20Set-up%20Transfer%20and%20Closure/Downloads/PDF/Final%20Government%20Response.ashx

[3] http://www.mbie.govt.nz/info-services/business/business-law/incorporated-societies

confidence that the persons listed as directors are legitimate people.

4 What are your views on the proposed objectives for assessing whether to introduce a director identification number?

The proposed objectives provide a good set of criteria for which to assess whether a director identification number should be introduced. Consequently, we agree with the proposed objectives.

5 What are your views on the benefits and costs of a director identification number? Are there any other benefits, costs or risks?

We believe the benefits far outweigh the costs. At present we already have many identification numbers for other agencies. The use of an identification similar to RealMe would greatly improve operation of the Companies Register and trust in its accuracy.

We do not believe the existence of a director identification number would convey proof of qualification to be a director any more than the present system does.

In addition, providing that there is sufficient regulation to prevent the linking of information using the identification number, and the system used to administrate it is secure, privacy concerns can be alleviated.

In relation to identity theft, to the extent this is a risk it could be minimised if the director's identification number was not displayed publicly. People would be able to find all the companies a director is registered against by clicking on their name on one company which would return a list of all the companies that director is a director of.

6 Do you support the introduction of a director identification number?

Yes.

7 If a director identification number is introduced, what are your views on how a number could work?

We agree with the proposed plan, however, we believe further associated changes could also be implemented. Currently the onus is on the Board of a company [4] to update the companies register if they become aware of a change of a director's address within 20 working days. We believe this requirement should be placed upon individual directors and any change in address should be made within 5 working days. We also believe failing to comply with this requirement should be considered an offence under the Companies Act 1993 as a deterrent and subject to a suitable penalty on conviction.

We also believe that directors should be obliged to keep other personal contact information up-to-date such as contact phone number and email address as part of the director identification number process. We believe that this additional information should only be available to the Registrar of Companies, the companies to which the director is appointed and a liquidator/administrator/receiver appointed to a company to

[4] Section 159(b) of the Companies Act 1993

alleviate privacy concerns but ensure compliance issues can be more easily communicated and enforced.

8 Do you have any other comments?

No.