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**“THE NEED FOR A VOLUNTARY
ADMINISTRATION REGIME
IN NEW ZEALAND”**

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CONTENTS PAGE:

I. EXAMINE WHETHER THERE IS A NEED IN NEW ZEALAND FOR ANY FORM OF CORPORATE RESCUE PROCEDURES(S):

A. THE NEED FOR ANY CORPORATE RESCUE PROCEDURE AS A MATTER OF POLICY;

1. A working definition of 'Corporate Rescue'

(a). Informal rescue

2. Why provide society with a corporate rescue mechanism?

3. Identifying Corporate Failure

4. Regulation of corporate failure in the New Zealand environment

5. Whether it is appropriate to use Insolvency Law as a vehicle for regulating corporate failure in this manner?

6. The need for any "Corporate Rescue" procedure, especially a Voluntary Administration regime as a matter of policy:

7. What are the failings or gaps in the current legislative procedures?

(a). PART XIV; COMPANIES ACT 1993:

(i). Outline of Part XIV's key provisions

(b). How far does Part XIV go in providing an adequate procedure for facilitating company rescues?

(c). Rationale behind the Joint Insolvency Committee recommendations:

(d). Alternatives to Part XIV Companies Act 1993 modifications:

(e). CORPORATIONS (INVESTIGATION & MANAGEMENT) ACT 1989:

(f). Examine its history and limitations:

(g). This aspect has many features of a rescue procedure:

(h). Who can initiate 'Statutory Management'?

(i). The justification of a 'statutory management' regime in New Zealand:

8. New Zealand's current position:

9. Conclusion

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I. EXAMINE WHETHER THERE IS A NEED IN NEW ZEALAND FOR ANY FORM OF CORPORATE RESCUE PROCEDURES(S):

A. NEED FOR ANY CORPORATE RESCUE PROCEDURE AS A MATTER OF POLICY;

1. A working definition of 'Corporate Rescue'

'Corporate Rescue' can be likened to a continuum with aversion to corporate¹ failure at one end of the spectrum, due to actively participating in a scheme of intervention or prevention. At the other end would be a statutory or formal legal rescue procedure which would usually be triggered by some defined, objective, threshold test of 'insolvency'² being met by the company³ or corporation⁴.

¹ Includes subsidiaries of companies. Corporate has the same definition as 'corporation' as set out in section 2 pursuant to the Corporations (Investigation & Management) Act 1989.

² In New Zealand for example, the Companies Act 1993 specifies that for a company to be put into either liquidation or a creditors compromise arrangement, the 'proponent' (can only include the company directors, creditors or shareholders with leave of the court; a receiver; or a liquidator pursuant to section 228 of the Act). of a compromise under a Part XIV creditor's compromise arrangement has to satisfy the test that the 'company is or will be unable to pay its debts' within the definition given to that phrase in section 287 of the Act. A presumption will arise if section 287 is satisfied upon evidence introduced into court but it is rebuttable presumption, and can be displaced by evidence to the contrary. This test may also apply to liquidations under section 240 (4)(a) upon a court appointed liquidator being appointed pursuant to section 244, under this section the liquidator is required to call a meeting of the company creditors if the liquidator is satisfied that the company is 'not able to pay its debts' pursuant to section 287 (Refer to section 244 (1)(b) of the Act).

³ 'Company' has been defined in New Zealand by the Companies Act 1993 in section 2 as a 'company registered under Part II of that Act and thus incorporated with the registrar of companies in accordance with the Companies Reregistration Act 1993'.

⁴ 'Corporation' is defined in section 2 of the Corporations (Investigation & Management) Act 1989, the definition is inclusive and includes subsidiaries of groups of companies.

Corporate rescue has been defined by many jurisdictions in a myriad of different ways⁵ attempting to deal with such financially distressed entity's within the confines of this continuum generally.

(a). Informal Rescue:

'Informal Rescue' refers to measures that can be taken without commencement of any formal insolvency procedures. What is required will vary from company to company, and will depend on the stage of distress. The directors themselves, or the company's bankers, any response to warning signs in the accounts, or some extrinsic factor may trigger action (for example collapse of a subsidiary or major customer). In either case, after the introduction of wrongful trading provisions in both the UK Insolvency Act 1986, section 214 and in section 135 of the New Zealand Companies Act 1993⁶. Also the increased scope of legislation in both the UK and New Zealand, to combat unfit directors⁷ both the bankers and the directors themselves should react sooner rather than later. It may be that the result of the UK 1986 legislation has encouraged earlier moves towards formal rescue in order to protect directors and their advisers.⁸ Ordinarily the company's constitution will include a power to compromise or modify the rights of creditors and shareholders, or classes of each. In New Zealand this is legal so long as the

⁵ Some methods of rescue along this scale can include the following:

A situation where the company itself will be liquidated but the undertaking or the actual business may be rescued by timely intervention by a third party; or a situation where the company strikes up an informal bargain with its creditor's enabling it to: reschedule its debts or refinance itself for an interim period and thus keep trading; new arrangements for changes in the management and personnel structures; the identification of core business and sale of loss-making or peripheral activities; reorganisation; and the injection of new capital.

⁶ Refer to section 135, Companies Act 1993 which deals with 'Reckless Trading' by the director of a company. It is a statutory requirement that a company director must not agree to or allow or cause the business of the company being carried on in a manner that is likely to create a substantial risk of serious loss to the company's creditors.

⁷ Company Directors Disqualification Act 1986, section 6 replacing s300 Companies Act 1985 (Insolvency Act 1985, schedule 10). See Sealy, *Disqualification and Personal Liability of Directors* 3rd edition, (CCH, 1991). See also section 169 Companies Act 1993 which allows New Zealand shareholders to bring personal actions against company directors for a breach of their duties owed under the company's act including their general duties owed under sections 131-138 of the act.

⁸ Refer section 251 Insolvency Act 1986 and see Lingard, *Corporate Rescues and Insolvencies*, 2nd edition (Butterworths, 1989).

constitution is not inconsistent with the legislation enacted in the Companies Act 1993⁹. However, there is an express legislative power to effect compromises with company creditors which can possibly amount to a variation of rights.

2. Why provide society with a Corporate Rescue mechanism?

'Corporate Rescue' has often been described as a countries legislative response to 'Corporate Failure'¹⁰. The scale of the failure will generally dictate the rescue regime and principles to be adopted to deal with the problem¹¹. In New Zealand in receiving any form of corporate rescue regime, the government was first forced to pose and address the simple question of "whether or not parliament wants to actually prevent or cure corporate failure?". This is in essence a policy consideration for the legislators to decide. It was also a relevant enquiry for them to decide just how far New Zealand was willing to go in promoting the type of 'rescue-culture' to which Lord Browne-Wilkinson referred in *Powdrill v Watson*¹².

In New Zealand since the election of the Labour Government in July 1984, New Zealand has adopted the free market approach or philosophy and moved from

⁹ Refer to section 31 which discusses the effect of having a constitution upon a company registered under the Companies Act 1993 in New Zealand. Refer also to section 26 to 34 which deals with the rights, obligations and duties which arise upon using a constitution in a New Zealand company.

¹⁰ See Argenti, *Corporate Collapse: The causes and symptoms*, McGraw-Hill, London, 1976, pg. 122, pp145-147. English writer Argenti identified 12 elements which he postulated were linked together in most corporate collapses: management, accountancy, information, change, constraints, overtrade, big project, gearing, financial ratios, creative accounting, non-financial symptoms, and the last few months.

¹¹ This is a salient consideration in New Zealand which was one of the cornerstone justifications behind the Corporations (Investigation and Management) Act 1989, the draconian mandatory moratorium provision which runs for an indefinite period and the political initiation requirements are only merited by the fact that the regime only applies to major corporations with several hundred interlocked companies and subsidiaries. Such failures that are viewed by the Securities Commission as potentially being likely to cause economic harm and hardship to our economy and the business community are put into the scheme without consultation or a court right to decline the regime. Such high level cases are segregated and investigated separately to determine if any corporate crime or money laundering took place within the corporations accounting sand financial records by the use of auditors; or if the corporation and its directors had traded without fraud or recklessness; if the directors had complied with all their reporting obligations under the Financial Reporting Act 1993 and the Financial Transactions Reporting Act 1993; and that the company directors did not breach any of their general duties pursuant to sections 131-138 of the Companies Act 1993. The Act seeks to identify any perpetrators of such crimes and trace any assets or laundered funds that they might have to contribute to the creditors pool or debts of the company.

¹² *Powdrill v Watson* [1995] 2 All ER 65, 76; [1995] 1 BCLC 386, 397 (H.L).

being one of the most regulated economies in the democratic western world to being one of the least regulated economies. So generally levels of government activism regarding state intervention to 'rescue' financially distressed businesses has been gradually subsiding. In the past the government dealt with particular corporate collapses in special legislation¹³ and to some extent still does with the continued use of statutory management regimes under the Corporations (Investigation & Management) Act 1989¹⁴ and the Reserve Bank of New Zealand Act 1989. These pieces of legislation have high threshold requirements¹⁵ and are designed to deal with the 'worst case scenario' type of corporate rescues. They operate only at a very high, specialised level and only to very specific scenarios, that involve content with potentially high economic or political repercussions for our society. Most ordinary company rescues would not fall within the confines of these jurisdictions due to the size and scale of such business entities not justifying the time and cost considerations involved in a statutory management being instituted.

¹³ See Cornish Companies Management Act 1974; Public Service Investment Society Management Act (No. 2) 1979.

¹⁴ Hereafter 'CIM Act 1989'.

¹⁵ For example, pursuant to the Corporations (Investigation and Management) Act 1989, section 38 (1) (a). The governor-general may, from time to time, by Order in Council, on the advice of the minister given in accordance with a recommendation of the Securities Commission, - (a). Declare that - (i). Any corporation: (ii). Any associated person of that corporation, - is subject to statutory management; and (b). Appoint one or more persons as statutory manager or statutory managers of that corporation or associated person.

Under the CIM Act 1989 the governor-general has this power, only upon the advice of the Minister, which must be given in accordance with a recommendation received by the Securities Commission for statutory management under section 39. Such a recommendation would only be made if the following considerations were salient factors in the enquiry: a complex group of companies linked by shareholdings or inter-company debts; many creditors, unsecured or holding a range of different securities, affecting different companies in the group; no security document enabling the timely appointment of a receiver or manager for the group as a whole; vulnerable assets; the prospects of protracted litigation and expense to trace rights through a complex group; the effect on a market of the possibility of uncoordinated and distressed sales; the effects of intervention and non-intervention upon the credit standings of New Zealand companies made by the Securities Commission to declare that any corporation or associated person be made subject to statutory management and that statutory managers be appointed. Where that power is exercised, every subsidiary of that corporation will also be subject to statutory management unless otherwise declared.

In Paul Heath's seminar paper "*Voluntary Administration - Proposals for New Zealand*"¹⁶ the writer put forward a new theory and he concluded that New Zealand's current law presently combines elements of capitalist philosophy and pragmatism. Heath did not see these two terms as laid out by Professor Flessner¹⁷ as mutually exclusive. He recognised that inherent to the concept of capitalism, was Darwin's rule of the '*survival of the fittest*'. He went on to explain that in a capitalist system like New Zealand, the resources of such a society are required to be transferred from one inefficient or failing application to another more useful trading entity. By the decline and failure of companies that are not operating or using its resources effectively and efficiently and by the rising success of companies that are viewed by capitalism as operating optimally, society will gain overall by a more cost effective and efficient business community, and by the greater options to trade competitively internationally. By parliament tampering with this area of the law, and reducing the number of failures, they are effectively damaging the efficiency of capitalism. As Heath stated, governments should be trying to use new rescue mechanisms, not to prevent all failures blindly, nor mindlessly to increase them, but to '*regulate*' failure, in order to improve the efficiency of capitalism as a means of allocating the resources of our society. However, due attention to possible consequential hardship and harm to vulnerable members of society should always be a salient consideration for our legislators.

3. Identifying Corporate Failure

As a side issue in the policy arena, Paul Heath also identified the need to identify the causes and symptoms of corporate failure in helping a government to

¹⁶ "*Voluntary Administration - Proposals for New Zealand*", see *Essays on Corporate Restructuring and Insolvency*, by Charles Rickett, Brooker's Ltd. 1996, pp 91-119.

¹⁷ For a discussion of the four basic philosophies of business insolvency law, namely pragmatism; government activism; capitalist; and enterprise philosophy. See John Farrar's seminar paper entitled "*Voluntary Administration in Australia and the United Kingdom - A comparative study*". See *Essays on Corporate Restructuring and Insolvency*, by Charles Rickett, Brookers Limited 1996, pp 69-90. John Farrar identified these four basic philosophies from a paper entitled "*Philosophies of Business Bankruptcy Law: An international overview*", by Professor Axel Flessner, see Ziegel (ed), *Current Developments in International and comparative Corporate insolvency law*, Clarendon Press, Oxford 1994, chapter 2.

determine whether or not to adopt an insolvency regime, and if so which one. English writer Argenti¹⁸ recognised twelve overlapping causes of corporate failure. A related consideration for our government and economists must then surely be the question of 'whether or not the New Zealand parliament, given our current economic, social and political policies and insolvency law philosophies; wants to prevent or cure such failures? or on the contrary, should they be aiming to increase the failure rates?'. The New Zealand government should aim to use such a corporate rescue mechanism in a way that will regulate company and business failures, in their discretion¹⁹ in order to improve the efficiency of capitalism. The Corporations (Investigation and Management) Act 1989 already goes a fair way towards striking such a balance and is very discreet in its application to any corporations operating in New Zealand. It regulates failure by being selective in its considerations for possible candidates of corporate rescue.

4. Regulation of corporate failure in the New Zealand environment

In any corporate rescue regime a side effect is the regulation of corporate failure and in designing such a mechanism the legislators have to decide what type of failures they want to prioritise in rescuing and what type of companies are more valuable to society as a whole and worth investing the time, money and effort in rescuing (for employment, investment reasons etc.). In New Zealand it is clear that corporations and their related subsidiaries have a type of rescue procedure

¹⁸ Argenti, *Corporate Collapse: The Causes and Symptoms*, McGraw-Hill, London 1976, p122. Pp145-147. He postulated the 12 causes as:

*"...If the **management** of a company is poor then two things will be neglected; the system of **accountancy information** will be deficient and the company will not respond to **change** (some companies, even well managed ones, may be damaged because powerful **constraints** prevent the managers making the responses they wish to make). Poor managers will also make one of three other mistakes, they will **overtrade**; or they will launch a **big project**; or they will allow the company's **gearing** to rise so that even normal business hazards become constant threats. These are the chief causes, neither fraud nor bad luck deserve more than a passing mention. The following symptoms will appear: certain **financial ratios** will deteriorate, but, as soon as they do, the managers will start **creative accounting** which reduces the predictive value of these ratios and so lends greater importance to **non-financial symptoms**. Finally, the company enters a characteristic period in its **last few months**."*

called '*statutory management*' available under the CIM Act 1989²⁰ however this Act is designed to deal only with multinational corporations and not closely held companies or one person company's. The statutory management regime requires a recommendation from the Securities Commission before a company can be placed into the scheme. The Security Commission has already identified a policy²¹ regarding its discretion in recommending to the Minister of Justice that a corporation be placed into statutory management. The kinds of factors the Commission take into consideration in deciding to make such a recommendation are: whether a complex group of companies linked by shareholdings and inter-company debts are involved; many creditors (including unsecured) affecting different companies; no security document enabling the timely appointment of a receiver or manager for the group as a whole; the prospects of protracted litigation and expense to trace rights through a complex group; vulnerable assets, such as work-in-progress under construction or development contracts; the effect on a market of the possibility of uncoordinated and distressed sales; the effects of intervention and non-intervention upon the credit standings of New Zealand companies. So this Act is discreet in its application but effectively '*regulates*' the type of client it wants to deal with and upon such a regime applying, has total control in terms of a mandatory moratorium and the appointment of statutory managers to deal with the company in whatever manner it sees fit, for an indefinite period. The Act effectively removes the directors from any position of power and grants the statutory managers all the powers and authorities of the directors and of a receiver. This very draconian Act is only used in the most severe scenarios, but in effect, it has achieved its purpose of effectively regulating the greatest corporate failures. This Act however, effectively cuts out ninety percent of companies operating in New Zealand. However Part XIV of the Companies Act 1993 sets out

¹⁹ The government should not use corporate rescue mechanisms to provide blanket coverage to all company's who apply for corporate rescue thus preventing all failures, nor should they mindlessly try to increase them. Regulation is the key.

²⁰ See Part III of the Corporations (Investigation & Management) Act 1989 which deals with the administration of the statutory management regime.

compromise arrangements that can voluntarily be entered into between a company's board of directors, its creditors and shareholders. This can have a similar effect to a rescue. But it is a voluntary regime initiated by the company directors in reality. It is not a court or government instituted scheme. The only real input the judiciary may have is that if the court has initiated the regime they may appoint a chosen nominee to draft a company voluntary administration proposal (includes a company director) who will present it to the company creditors at the creditors meeting. Upon its approval the nominee will report it to the court. However such a plan does not require any input, recommendations, commentary or approval from the court. It is merely a reporting function. I agree that a voluntary arrangement scheme like the one in existence in New Zealand under Part XIV of the Companies Act 1993, should be flexible, and informal, without court intervention. I believe it is operating effectively. However the differential between the formality of the above two Acts highlights the need for an intermediary piece of legislation. A voluntary administration scheme as the Joint Insolvency Committee recommended may well fill in the gap and provide a form of regulation for this area of the law the legislators have not yet addressed. The fact that no mandatory formal rescue regime effectively addresses the majority of closely held companies in a similar fashion to the UK's Administration Order regime emphasises the need to legislate for such a regime, to enable the courts to regulate this area of the law more effectively.

5. Whether it is appropriate to use Insolvency Law as a vehicle for regulating corporate failure in this manner?

But still the issue remains of "whether it is a valid role of insolvency law to regulate failures in this manner". It has certainly been debated by many writers as to whether regulating this area of the law, namely corporate recoveries, is actually a basic first principle of insolvency law and therefore a role that insolvency law

²¹ See 'Statutory Management: Report to the minister of Justice on Part III of the Corporations (Investigation & Management) Act 1989', Wellington, Securities Commission, April 1992.

should be aiming to fulfill at all. There is however room to argue if this should be a principle because no 'fresh start' policy applies to company's in New Zealand. Here, individual bankrupts are automatically discharged after three years pursuant to section 107 of the Insolvency Act 1967²². This provision releases the bankrupt from all their 'provable debts'²³ owed to any unsecured creditors they may have. After such a discharge, the individual bankrupt under the policy of a 'fresh start' can start over again because his credit slate is wiped clean. This approach does not apply to company's in New Zealand because in policy terms, they are not human but are abstract entities and it does not matter as much in terms of public policy if they are dissolved. Companies have a separate legal personality²⁴ and limited liability²⁵ and thus the share-holders can only ever be held liable to the extent or price of their shares. The only exceptions to his limited liability rule is if the share-holders have not paid for all the price of their shares but have deferred payment²⁶ or if one can find a director liable²⁷, then such a director will be held personally liable to contribute to the assets of the company. Members are otherwise not liable for the companies debts under this principle. It has been recognised, as mentioned earlier, that it is not efficient according to the capitalist philosophy, to rescue a company in every case, some have to fail because they are not using their resources wisely, effectively and operating efficiently and thus not contributing positively to society. Thus on a policy basis I would argue that this principle is a relevant enquiry to the New Zealand government given the fact that our laws are applied to a business environment that operates under predominantly capitalist and pragmatism philosophies. Secondly, such a corporate rescue principle has already been endorsed as a basic principle of New Zealand insolvency law, given the adoption of the Corporations (Investigation and Management) Act 1989 and its predecessors in the form of the Companies Special Investigation Act 1958 and

²² There are exceptions to section 107 like fraud.

²³ 'Provable Debts' are those existing at the time of the adjudication and can include future and contingent debts.

²⁴ See section 15, Companies Act 1993.

²⁵ See section 97, Companies Act 1993.

²⁶ See section 97 (2)(a), Companies Act 1993.

1934, and Part XIV of the Companies Act 1993. Thus such a principle has already been endorsed through corporate rescue legislation in place and operating effectively within the New Zealand insolvency law environment. So I conclude that it has already become an implied role of our insolvency laws to regulate corporate failures through corporate rescue legislation already in existence, in a manner that is consistent with New Zealand's dominant business philosophies of capitalism and pragmatism. Thus our system allows many smaller businesses to fail but larger corporations whose failure would adversely effect our economy and job market are placed into statutory management and rehabilitation plans and rescue options formulated to financially rescue such businesses. Thus our government is already regulating the companies it allows to fail and those it attempts to save from financial disaster. Such regulation has been based upon a cost-benefit analysis and governmental budget restraints and other such considerations; which include the company's worth to our society, socially (for employees etc.), economically, politically (political parties election campaign promises to the New Zealand business community), etc.. and the time and costs involved for our government in rescuing such a company.

6. The need for any "Corporate Rescue" procedure, especially a Voluntary Administration regime as a matter of policy:

Currently the only forms of corporate or company rescue regimes that are available in New Zealand are under Part XIV²⁸ and Part XVI²⁹ of the Companies Act 1993, receivership under the Receivership Act 1993 and statutory management under the Corporations (Investigation & Management) Act 1989. Because New Zealand has not yet undertaken a reassessment of its corporate insolvency laws, it has not yet followed the trend of its UK and US counterparts in adopting a voluntary administration system into its legislation. So I will now identify the gaps in the

²⁷ See section 97 (2)(c.), Companies Act 1993.

²⁸ Part XIV, Companies Act 1993 deals with voluntary compromises between a company and its creditors.

²⁹ Part XVI, Companies Act 1993 deals with liquidation of a company registered under the Act in New Zealand.

New Zealand legislation by focusing especially upon Part XIV of the Companies Act 1993 and the CIM Act 1989.

7. What are the failings or gaps in the current legislative procedures?

In New Zealand the trend to adopt something akin to the Australian system of 'Official Management'³⁰ has often been stalled due to New Zealand's cautious nature in regard to their cost-benefit analysis. In 1980 the Minister of Justice³¹ commented that the 'Creditor's Management' provisions were dropped because they were seriously considered to be insufficient in meeting their stated purpose³². Also of concern was the fact that such a mechanism could potentially become a vehicle for abuse by companies or creditors attempting to delay liquidation proceedings from commencing.

The concept of 'Voluntary Administration'³³ however was supported as a viable option to parties which could streamline the process available under section 205 Company's Act 1955 which was viewed as 'cumbersome, costly and difficult to implement'³⁴. As a result by June 1989 the Law Commission recommended that a system of 'voluntary administration' of company's in or apprehending financial difficulty was 'desirable'.³⁵ The Securities Commission³⁶ also stated that the statutory management regime should be retained but that further review of the law dealing with insolvent and at risk corporations should be undertaken.

³⁰ Known as 'Creditor's Management', such a scheme for company's were introduced in the Companies Amendment Bill 1979, clause 42, into the New Zealand parliament in 1979 and was dropped.

³¹ Hon. J K McKay upon moving the second reading of the bill.

³² The minister based his opinion heavily upon the Australian Official Management statistics, especially New South Wales where over the past 10 years, of 30 companies, only 1 or 2 were rehabilitated.

³³ New Zealand currently has a hybrid type of voluntary creditors compromise arrangement available under Part XIV Companies Act 1993, which followed in essence its predecessor s205 Companies Act 1955. However New Zealand as of yet has nothing akin to the UK's Administration Order regime.

³⁴ See *Report of the New Zealand Law Society Committee on Insolvency Law Reform* (July 1989) para 1(e) p2; see also submission to the Law Commission on Insolvency Law Reform by the New Zealand Society of Accountants; August 1988, at p.2 and pp 1-7 of the appendix to those submissions.

³⁵ See *Company Law: Reform and Restatement*, NZLC R9, New Zealand Law Commission, Wellington, 1989.

³⁶ See *Statutory Management, Report to the Minister of Justice on Part III of the Corporations (Investigation & Management) Act 1989*, Securities Commission, April 1992.

As a result the 'Joint Insolvency Committee'³⁷ was established by the New Zealand Law Society and the New Zealand Society of Accountants who issued provisional recommendations on whether a voluntary administration regime should be adopted in New Zealand.³⁸ The JIC recommended reform and modification of Part XIV of the Companies Act 1993 be undertaken to accommodate the voluntary appointment and use of an administrator, also requirements for an independent report and full moratorium provisions to apply if an administrator³⁹ is appointed. A side issue that was also considered was the voting rights and requirements to determine such a compromise agreement. The JIC in issuing these provisional provisions believed that they had struck the right balance between protecting the rights of secured creditors, who may otherwise be made subject to a moratorium and the need for a moratorium to assess adequately whether rehabilitation and sale of a business as a going concern is viable. Their recommendations for a modified voluntary administration scheme under Part XIV was consistent with existing company law and basic principles of insolvency law generally in New Zealand.

³⁷ Hereafter 'JIC'.

³⁸ See Provisional Recommendations of the Joint Insolvency Committee (7th October 1994) subsequently Mr R. Dugan has prepared some draft legislation for the committee to consider but matters have been put on hold pending the Ministry of Commerce's assessment of business law priorities. Ms Lucy Dome from the Ministry commented that the reforms framework draft paper will be going back to Insolvency laws first principles and a draft framework paper will be in circulation for the Ministry of Commerce internally by February 1998. All such documents are currently being withheld from the public pursuant to the Official Information Act 1982. However the Ministry of Commerce's objectives include:

To minimise the costs related to creditors associated with insolvency by providing a mechanism for creditors to enforce repayment obligations which encourages debtors and creditors to act in a manner which:

- (a) maximises the amount repaid to creditors; and*
- (b) minimises the total costs associated with obtaining that repayment.*

To distribute the losses associated with insolvency in a manner that is consistent, where possible, with the objective set out in paragraph 1.

To enable individual debtors who are insolvent to continue to participate effectively in the economy and society by discharging them from their debts in appropriate circumstances.

To provide an institutional framework to achieve these objectives which:

- (a) Is capable of being applied and administered in a predictable and cost-effective manner; and*
- (b) minimises the costs incurred in complying with it.*

To resolve any conflict between these objectives in a manner which is most consistent with enhancing:

- (a) the incentives for individuals and firms to allocate resources to their most productive use; and*
- (b) the ability of individuals and firms to respond to those incentives.*

³⁹ Such an administrator would have limited control over the company's affairs during this period.

They had based their research very heavily upon the UK⁴⁰ and Australian⁴¹ experiences.

Part XIV of the Companies Act 1993 provides a mechanism for a company to enter into a compromise⁴² agreement with its creditors, instead of an immediate

⁴⁰ The UK Company Voluntary Arrangement procedure is a modification of the section 425 creditor's scheme of arrangement regime. The procedure essentially enables a company to enter into a voluntary arrangement with creditors and shareholders under the supervision of a qualified Insolvency Practitioner. (sections 1-7 Insolvency Act 1986 UK). The directors of the company prepare a draft CVA proposal in consultation with their chosen nominee, who, if approved by the creditors, generally then becomes the supervisor of the rescue plan. There is no requirement that the company is insolvent at the time of making the proposal, so it can be used to avert a crisis.

⁴¹ The Australian Voluntary Administration Scheme was introduced into Australian law by the Corporate Law Reform Act 1992 (Commonwealth) which came into force in June 1993 as a result of recommendations contained in the 1988 report by the Australian Law Reform Commission on Insolvency, commonly known as the 'Harmer Report' after the Chairman of the Commission.

Echoing the Cork Committee, the Harmer Commission similarly recognised the shortcomings of traditional insolvency remedies, namely, receivership, court liquidation, schemes of arrangement and official management and acknowledged a need to provide a new alternative insolvency remedy that would overcome the deficiencies of traditional procedures and allow a more constructive approach to insolvency. Part 5.3 of the Australian Corporations Law states that the object of Voluntary Administration is:

"... to provide for the business, property and affairs of an insolvent company to be administered in a way that:

(a) maximises the chances of the company, or as much as possible of its business, continuing in existence; or

(b) if it is not possible for the company or its business to continue in existence - results in a better return for the company's creditors and members than would result from an immediate winding up of the company.

A 28 day moratorium, extendable up to 60 days with creditors agreement, comes into effect once an administrator is appointed. The moratorium generally imposes a stay upon the exercise of all rights against the company. Exceptions include allowing any fully secured creditor to commence enforcement within the first 14 days after the date of notice of the appointment of an administrator.

During the administration the powers of the directors and other officers are suspended in favour of the administrator as agent of the company. The administrator also has the power to dismiss or replace the existing directors. (Corporate Law Reform Act 1992, s473A and s473C.).

In contrast to the English CVA procedure, entry into the Australian procedure is notable for its lack of stringent and costly formalities, with no requirement of court involvement either by way of application or by way of filing.

⁴² See section 227 Companies Act 1993 which sets out the definition of 'compromise'. It includes cancellation of all or part of a debt of a company or variation of, the rights of a creditor, or the terms of a debt or any alteration to a company's constitution that affects the likelihood of the company being able to pay a debt. Such a proposal may be suggested when the proponent "has reason to believe that the company is or will be unable to pay its debts" within the meaning of s287 of the Companies Act 1993". By s287 a company is presumed to be unable to pay its debts if it has failed to comply with a statutory demand; if execution issued against the company in respect of a judgment debt has been returned

winding up of the business or company pursuant to a liquidation or receivership. It allows the board of directors time to sell the company as a 'going-concern', reschedule its debts, refinance or gain further finance; and attempt to trade out of its financial difficulties. Part XIV does not currently provide a moratorium on enforcement of securities in the period between the making of the compromise proposal and the approval reached at a meeting of the creditors. This would normally be the case for any company placed into statutory management by an order in council.⁴³ However the justification for the immediate mandatory moratorium under the Corporations (Investigation and Management) Act 1989 is that the corporate scenarios that the CIM Act 1989 is designed to deal with is vastly different to the majority of company failures that would arise under a part XIV provision in terms of size, scale and economic impact. Under Part XIV acceptance of a proposal is a matter for determination by creditors who are affected whereas statutory management is imposed upon creditors without a meeting and a court hearing. An automatic full moratorium would follow in extremely wide terms⁴⁴ whereas mentioned, there is no such equivalent part XIV provision for a moratorium during this interim period.

The JIC concluded that Part XIV contained flexible provisions which enabled compromises to be entered into a company and its creditors with a minimum of court intervention, involvement and formality. Also it was not seen to be in the interests of either the company or its creditors that the use of an administrator and the requirement to obtain an independent report be mandatory for all company compromises due to the significant time and costs involved. So the JIC concluded that Part XIV was flexible enough to be modified to include a much needed voluntary administration scheme, of which based upon the UK and Australian

unsatisfied in whole or in part; a person entitled to a charge over all or substantially all of the property of the company has appointed a receiver under the instrument creating the charge; or where a compromise has been put to a vote under Part XIV but has not been approved. S287 Companies Act 1993 presumptions of insolvency are rebuttable.

⁴³ See Corporations (Investigation & Management) Act 1989, section 42.

⁴⁴ See Corporations (Investigation & Management) Act 1989, section 42 (1).

experiences, was a sorely missed option in our insolvency laws and a much needed regulatory piece of legislation in the New Zealand environment.

(a). PART XIV; COMPANIES ACT 1993:

(i). *Outline of Part XIV's key provisions*

I will now outline the current provisions (as yet unmodified) of Part XIV of the Companies Act 1993 and attempt to identify the provisions of that regime which the Joint Insolvency Committee recommend be modified to accommodate New Zealand's first Voluntary Administration regime. Part XIV comprises of eight sections which provide a flexible mechanism by which a company can enter into a compromise arrangement with its own creditors. What cannot be achieved under the current provision, unlike in a statutory management scenario; is a moratorium on enforcement of securities in the interim period between the making of the compromise proposal and the approval at the creditor's meeting towards such a proposal or modified proposal.

The existing provisions of Part XIV embrace any form of compromise⁴⁵ between a company and its creditors; while inclusive in nature, the definition of the term A compromise proposal may be made by the board of directors of a company, a receiver appointed in relation to the whole or substantially the whole of the assets and undertakings of the company, a creditor or a shareholder⁴⁶ of the company or by a liquidator of the company.⁴⁷ A compromise may be put when the proponent of the compromise: "*has reason to believe that a company is or will be unable to pay its debts within the meaning of section 287 of this Act*".⁴⁸

⁴⁵ "*compromise*" extends to cancellation of all or part of a debt of a company or variation of the rights of a creditor of the company or the terms of a debt or any alteration to a company's constitution that affects the likelihood of the company being able to pay a debt.

⁴⁶ Companies Act 1993, s228(1)(d).

⁴⁷ Companies Act 1993, s228(1)(a)-(c.).

⁴⁸ Companies Act 1993, s228(1). By s287 of the Act a company is presumed to be '*unable to pay its debts*' if it has failed to comply with a statutory demand; if execution issued against the company in respect of a judgment debt has been returned unsatisfied in whole or in part; a person entitled to a charge over all or substantially all of the property of the company has appointed a receiver under the instrument creating the charge; or where a compromise has been put to a vote under Part XIV but has not been approved. The opening words to s287 Companies Act 1993 suggest that the presumptions of insolvency contained in that section are rebuttable.

The proponent of the compromise must however provide certain information to all creditors⁴⁹, liquidators, receivers and deliver such information in a prescribed form to the Registrar of Companies for registration.

A meeting is then convened in accordance with the Fifth Schedule to the Companies Act 1993. If the compromise (including any amendment proposed at the meeting) is approved by creditors, it becomes binding on the company and on all creditors (or, if there is more than one class of creditors, on all creditors of that class) to whom the notice of proposal given under s229 of the Act.⁵⁰

After approval by creditors, a compromise may be subsequently varied.⁵¹ The High Court has certain powers to give directions of a procedural nature or to order a stay of proceedings or to prevent a person from taking measures to enforce payment of the debt in the period between notice being given and notice of the result of voting at the meeting; however, secured creditors cannot be affected by such orders.⁵²

(b). How far does Part XIV go in providing an adequate procedure for facilitating company rescues?

Part XIV is not effective in that such a regime can be thwarted upon the dissent of creditors at the meeting, the simple filing by one creditor for a receiver or a liquidator. It is a system that is too dependent upon creditor agreement to compromise or risk their secured rights. Such an attitude can only be viewed as naïve in the commercial business environment. I would assume that based upon the theory of human self interest, the probability of one creditor not agreeing to such a measure is likely. Thus an alternative system is required to address a situation where the majority of creditors wish to rescue a company but one major creditor does not. An administration regime might be viewed as a more viable option to such a creditor.

⁴⁹ Companies Act 1993, s229.

⁵⁰ Companies Act 1993, s230.

⁵¹ Companies Act 1993, s231.

⁵² Companies Act 1993, s232(1) and (2). The Court also has powers to make orders that certain creditors are not bound in the event of irregularities: s232(3). The Court also has powers to give directions as to the

(c). Rationale behind the Joint Insolvency Committee recommendations:

The Joint Insolvency Committee took the view that Part XIV contained flexible provisions which enabled compromises to be entered into between a company and its creditors with a minimum of court involvement and formality. Yet, two features of the Australian voluntary administration regime were to be found in (or incidental to) Part XIV of the Companies Act 1993 Act. First, under s287(d) rejection of a compromise proposal gives rise to a presumption of insolvency on which a creditor could base an application for the appointment of a liquidator. Secondly, under s232(1) the court has power to stay proceedings by creditors, but (contrary to the Australian system) s232(2) provides that this power cannot be exercised to prevent a secured creditor from enforcing a security.

In the view of the Joint Insolvency Committee it was not in the interests of either the company or creditors that the use of an administrator and the requirement to obtain an independent report be mandatory for all company compromises because of the significant costs involved. There is nothing to prevent a person being appointed under a Part XIV compromise as something akin to an administrator; however such a proposal can be easily dissented to and overturned by company creditors; neither is there any proscription of the obtaining of an independent report. In some cases (but certainly not all cases) there may be good reason why the board of the company should remain in control of the affairs of the company. In other cases it will be appropriate for an independent administrator to be appointed with supervisory powers. Essentially it is a matter for the business judgment of creditors to determine whether an independent report and/or an administrator is required pending consideration of a proposed compromise by creditors.

In light of those considerations the Joint Insolvency Committee formed the view that it would be unnecessary, in current New Zealand conditions to enact

effect of the compromise if the company is subsequently placed in liquidation: s233. The Court also has powers to give directions as to costs incurred in the compromise procedure: s234.

additional provisions providing for a voluntary administration regime. Rather, the Committee took the view that Part XIV of the Act should be modified so that it could be used to accommodate a voluntary administration regime. This would mean that, under modified Part XIV provisions, a company which wished to propose a compromise to creditors could choose one of two options:

- (i). *First, those provisions in the modified Part XIV of the Act which are presently in existence could be used to effect a compromise in the manner which is presently contemplated by the Part XIV procedure; or*
- (ii). *Secondly, the provisions which are to be added to Part XIV of the Act to enable a full moratorium to be obtained could be used. If a full moratorium was desired, it would be necessary to appoint an administrator who could oversee the company's affairs until creditors had voted on the proposed compromise.*

If the second option were taken, it is proposed by the Joint Insolvency Committee that the board of the company would continue to have day-to-day control of the company and its affairs during the moratorium period which would enure until such time as creditors had voted on the proposal. During that period, however, the Committee envisages that the administrator would have powers of veto in relation to the sale of any fixed assets of the company and sale or disposition of any other assets (or the incurring of obligations) other than in the ordinary course of business. The primary duty of the administrator would be to monitor the operations of the company by the board, to investigate the affairs of the company and to prepare a report on the compromise proposed to be put to creditors by the company. In this way the administrator could be seen as independent from the board of the company.

So far as the length of a moratorium period is concerned the Joint Insolvency Committee's view was that, in most cases, 21 days would be adequate. However,

the Committee would favour the High Court being given the power to extend the period of the moratorium if good cause was shown.

Under the Australian legislation, secured creditors, owners of property and lessors cannot, without the consent of the administrator or the court, enforce their property rights during the 28-day period between the date of appointment of the administrator and the date of the creditors' meeting.⁵³ Further, under the Australian statute, a person holding a charge over all or substantially all of the assets of the company is able to appoint a receiver within 10 working days after it receives notice of the appointment of an administrator. If action is taken within that time, the powers of the receiver override those of the administrator.⁵⁴

Initially the view of the Joint Insolvency Committee was that a person holding a charge over all or substantially all of the company's property in this situation should be given 3 working days notice of the company's intention to make a proposal providing for the appointment of an administrator; this would give the charge holder the option to veto the appointment of an administrator by appointing a receiver.⁵⁵ In practice, it will be very rare for the charge holder not to be acquainted with the type of difficulties faced by the company prior to the time at which the 3 days notice is given. In addition the company will in practice require support for its debenture holder for any proposal for compromise that it wishes to make. I see this aspect as being an improvement over the position under Australian law where the receiver can be appointed subsequent to the administrator taking office and embarking upon detailed work.

The Joint Insolvency Committee has considered both the Australian and English legislation in making its recommendations. It is fair to say that our recommendations have been based on provisions in the Australian legislation rather than provisions contained in the English legislation. In essence, in order to

⁵³ *Corporations Law*, ss440B - 440C. Furthermore, during this period, all proceedings by other parties (including unsecured creditors) are stayed: s440F.

⁵⁴ *Corporations Law*, s441A. Generally, see O'Donovan, "Voluntary Administration Deeds of Company Arrangement Under Part 5.3A of the Corporations Law" (1994) 12 *Company and Securities LJ* 71, pp81-84.

maximise returns to creditors, the Joint Insolvency Committee sees a need not only to enhance the value of assets but also to minimise costs; to minimise costs it is important to keep Court involvement to a minimum.

(d). Alternatives to Part XIV Companies Act 1993 modifications:

Without intending to be exhaustive, the following are additional matters which the JIC⁵⁶ held needed to be considered if legislation is to be introduced to widen remedies available to companies in, or apprehensive of, financial distress.

(i). Parliament must address the question whether there is a need for additional powers to be available in the context of major corporate, banking, or insurance collapses. Parliament must also determine whether, if additional powers are considered appropriate, those powers should, as a matter of policy, be consistent with those remedies available under general insolvency law. At present, statutory management may be imposed upon banks⁵⁷ and corporations in respect of which there is evidence of "fraudulent or reckless conduct" or it has been determined "desirable" to administer the corporation under statutory management because that is more effective than any other form of insolvency administration.⁵⁸ An overall review of insolvency law will best enable these questions to be addressed: particularly the vexed question of how to deal (on insolvency) with groups of companies which have been (effectively) managed together as one.⁵⁹

⁵⁵ However, during the Committee's most recent discussions some members tended to the view that the Australian approach might be more desirable.

⁵⁶ See Paul Heaths paper 'Voluntary Administration - Proposals for New Zealand', see *Essays on Corporate Restructuring and Insolvency*, by Charles Rickett, Brooker's Ltd. 1996, pp 91-119.

⁵⁷ Reserve Bank of New Zealand Act 1989, ss117-158. For background, see *Krasemann v DFC NZ Ltd.* [1990] 3 NZLR 606.

⁵⁸ Corporations (Investigation and Management) Act 1989, ss38-75. See generally *McDonald v AGC (NZ) Ltd.* [1990] 1 NZLR 227. See also the provisions for judicial management of insurance companies in distress in the Life Insurance Act 1908, ss40A-40Q and *Re ACL Insurance Ltd.* [1991] 1 NZLR 211.

⁵⁹ For a brief review of the present position in that regard see Heath, "Group Insolvencies in New Zealand - Pooling and Contribution Orders" (1994) *International Insolvency and Creditors Rights Report* 17 (Vol. 6, No. 2); see also, generally, *Re Dalhoff & King Holdings* [1991] 2 NZLR 296.

(ii). *The taxation implications of any insolvency regime designed to enable a company to continue trading (either for the purpose of rescue or better realisation of assets by a sale of a business as a going concern) must be addressed. Specifically, those provisions of the Income Tax Act 1976 which may create taxation liabilities under the accruals regime need to be considered in the context of legislation designed to benefit creditors.⁶⁰ Parliament needs to determine which is more desirable: the generation of revenue or the rescue of a company (at one end of the scale) or (at the other end of the scale) the maximisation of returns to creditors on the sale of a business of a company in financial distress. Prudent business people will always have the taxation consequences of a decision in mind when determining how to approach a proposed compromise.*

(iii). *It may be necessary to re-assess duties of directors of companies from both civil and criminal perspectives. If a company is in financial distress it may well be prudent for directors to seek compromises with creditors. Specific defences may be considered rather than trading on the company with the possibility of serious harm to creditors. Some thought needs to be given to that possibility. Under Australian law it can be a defence to a civil penalty order proceeding for insolvent trading if the directors put the company into administration.⁶¹*

⁶⁰ Income Tax Act 1976, s64F (1)(ii). See also s188 which deals with group taxation issues.

⁶¹ Corporations Law, s 588H(5) and (6). See Crutchfield, *Corporate Voluntary Administration Law*, Law Book Company, Sydney 1994, p25.

(e). CORPORATIONS (INVESTIGATION & MANAGEMENT) ACT 1989:

(f). *Examine its history and limitations:*

The current CIMA 1989 was based upon the Corporations (Special Investigation) Act 1934⁶² which provided for the orderly investigation of affairs of a large number of intertwined companies by the appointment of a statutory receiver with wide powers. The CSI Act 1934 was enacted to protect investors in shares, debentures, bonds, security certificates "and other like instruments" issued by the companies listed in the schedule to the Act and by companies added to that schedule at a later date. The CSI Act 1934 conferred powers on inspectors appointed by the governor-general to investigate the affairs to those companies. The CSI Act 1934 also involved the institution of a moratorium upon the commencement or continuation of proceedings without leave of the court; and also extended powers upon the court in winding up proceedings so as to provide for the equitable distribution of the remaining assets. It was special legislation rushed through parliament in response to a particular commercially disastrous situation⁶³. One can argue that Statutory Management thus arose from pragmatism. Similar legislation was subsequently enacted in the Cornish Companies Management Act 1974, the Public Service Investment Society Act 1979, and the Reserve Bank of New Zealand Amendment Act 1986. These pieces of legislation all referred to the term 'statutory manager' rather than 'statutory receiver'. The CSI Act 1934 was repealed by the Companies Special Investigations Act 1958⁶⁴. When the CIMA

⁶² Hereafter 'CSI Act'. The CSI long title to the 1934 Act is stated as: "An Act to give effect to certain recommendations made by a Commission appointed under the Commissions of Inquiry Act 1908, in relation to Companies and other Corporations that seek to raise capital and loan funds in New Zealand".

⁶³ Refer to Richardson J., in *Hawkins v. Davison* (1991) 5 NZCLC 66,910 at page 66,916 affirming the decision of Wylie J. in the High Court reported sub nom *Hawkins v. Minister of Justice* [1990] 3 NZLR 486.)

⁶⁴ The Companies Special Investigations Act 1958 ("the CSI Act") repealed the 1934 Act, the Companies (Temporary Receivership) Act 1934 and the Companies (Special Liquidations) Act 1934, and consolidated the investigatory, receivership and liquidation elements of the earlier legislation into one Act.

1989 received the Royal Assent on 22nd March 1989. Commenting upon that bill⁶⁵ the Minister of Justice, the Rt Hon G W R Palmer said:

"... The purpose of the Bill is to update and replace the [CSI 1958 Act]. The Bill arises from a review of the Act that I asked my department to undertake urgently in the light of recent company failures and the corporate fraud debate that has occupied so much of the House's time in recent months... In practice the Act has, in the main, been used in cases when a group of companies has been run as one company or when a group's affairs are so inextricably intertwined that the ordinary procedure of placing each individual company in the group in a separate receivership or liquidation would be cumbersome, unrealistic and time-consuming".

At the second reading of the Bill⁶⁶, the minister addressed the need for such legislation commenting that the commercial community's deteriorating standards of commercial conduct and the consequential public concern about such matters has resulted in the need for the CIMA Bill 1989. He cited the Equitycorp case which involved hundreds of separate companies of an interlocking variety, as one reason for enacting the new Bill. The general principles and powers contained in the CIMA 1989 are essentially the same as those contained in its 1958 predecessor with the only salient difference being the fact that secured creditors may not exercise their rights to realise their security without the consent of a statutory manager.

(g). This aspect has many features of a rescue procedure:

'Statutory Management' is available in New Zealand under two pieces of legislation, the Corporations (Investigation & Management) Act 1989⁶⁷ and the Reserve Bank of New Zealand Act 1989. Since these two acts came into force,

⁶⁵ See *Hansard*, 13th September 1988, pp 6493-6494

⁶⁶ See *Hansard*, 29 February 1989, page 9154 - 9155.

⁶⁷ Hereafter 'CIMA 1989'.

most of the criticisms have been directed on the moratorium against the enforcement of securities issue and the exercise of set-off rights and the consequential loss of control and access by a secured creditor to the debtors assets. However, overall the CIMA 1989 have been retained irregardless, upon the recommendations of the Securities Commission⁶⁸ because of the success enjoyed by the Act with some of its past major statutory management's⁶⁹. The object of the Act is set out in section 5⁷⁰. The Act applies to any 'corporation'⁷¹ that is or may be, operating 'fraudulently or recklessly'⁷², or to which it is desirable that the Act should apply to protect the interests of members, creditors, or beneficiaries or the public, if such interests cannot be adequately protected under the law. The statutory management provisions, as provided for in the Corporation (Investigation and Management) Act 1989, are significantly different from overseas legislation of its type. Specifically, the New Zealand legislation requires ministerial (political) involvement to be operative, unlike its international counterparts, and does not guarantee an input from creditors into the statutory management process, and does not give disaffected parties recourse to the court for resolving disputes. These

⁶⁸ See 'Statutory Management: Report to the minister of Justice on Part III of the Corporations (Investigation & Management) Act 1989', Wellington, Securities Commission, April 1992.

⁶⁹ In the 1980-1990 period, several major statutory management's were undertaken in regard to major corporations and their subsidiaries. For example, Equitycorp, Richmond Smart, and Chase (property) groups and the DFC Group. See Anderson's *Company & Securities Law*, Wellington, Brooker's, 1994 for a list of orders under this Act.

⁷⁰ Section 5, CIMA 1989 states such *objects* of the Act to be:

- (a) To confer powers on the Registrar of Companies to obtain information about, and to investigate the affairs of, corporations to which the Act applies;
- (b) In the case of a corporation that is or may be operating 'fraudulently or recklessly', to limit or prevent such conduct, or the effects of it, and the risk of further deterioration;
- (c.) To preserve the interests of the members, creditors, beneficiaries, or public if they cannot be protected adequately under the Companies Acts or in any other lawful way; and
- (d.) To provide for the affairs of corporations to which the Act applies to be dealt with in a more orderly and expeditious way.

⁷¹ See section 2, CIMA 1989, 'corporation' is defined widely to mean 'a body of persons, whether incorporated or not, and whether incorporated or established in New Zealand or elsewhere'.

⁷² See section 6, CIMA 1989 which defines 'fraudulently and recklessly' for the purposes of the Act, as a corporation that: (a). Contracts debts which the officers of the corporation did not, at the time the debts were contracted, honestly believe on reasonable grounds the corporation would be able to pay when they fell due for payment as well as all its other debts (including future and contingent debts); or (b). It carries on business or operates in a reckless manner; or (c.). It carries on any business or operates with intent to defraud its creditors or members or the creditors or members of any other person, or for any other fraudulent purpose".

differences are salient considerations for any international investors considering investing in New Zealand businesses.

The two most salient and immediate effects of a statutory management are the imposition of a mandatory automatic moratorium against various actions by creditors and claimants⁷³ and the vesting of the management of the corporation in the statutory managers⁷⁴.

(h). Who can initiate 'Statutory Management'?

In New Zealand the CIMA 1989 is initiated by organs of the state, not by the directors of the company's. One has to look at how simple it should be for initiating these proceedings. The salient issue then becomes 'What threshold of proof to put the company into the rescue procedure'? At one extreme, no court hearing should be necessary to trigger a moratorium just the action of the debtor filing into court for proceedings to commence (as in a company voluntary administration) and at the other end the court should be satisfied at some appropriate threshold of proof, that the procedure is going to be beneficial in some way (as is the case in England). Of course if the threshold is too high, then it may become costly for smaller company's to use (as is the case with New Zealand statutory management regime). Such management will terminate immediately upon the event of liquidation under Part XVI of the Companies Act 1993 or upon the

⁷³ See section 42, CIMA 1989 which deals with the 'moratorium'. It states it is broadly based and prohibits any pre-contractual claims or obligations prior to the statutory management (except those for the purpose of establishing validity); the enforcement of any judgment in respect of any of the above claims; or the recovery of property in the possession of the corporation; or the termination of, or re-entry or distraint for rent in respect of, any tenancy; or the exercise of any right of set-off against the corporation; or the enforcement of securities; and any application or resolution for liquidation. Section 42(4) specifically provides that the moratorium does not effect the 'existence of any security...or its priority over other debts'.

⁷⁴ See section 45, CIMA 1989 which deals with 'statutory managers'. The Act grants them very wide powers and displaces the powers of the corporations directors and officers (except to the extent a statutory manager allows, in his/her discretion). Under section 45 the management vests in such managers who are simultaneously given all the powers, rights and privileges of the corporation and generally given all powers, rights and authorities as may be necessary to carry out the powers conferred to them under Part III of the Act (see section 46). Additional and specific powers may be provided by other provisions also (see sections 46 - 59 generally). Pursuant to section 4 a statutory manager in exercising any such powers must have regard to the need to preserve the interests of members, creditors, beneficiaries, and the public

application for liquidation by a statutory manager or by an Order in Council. So by summary a corporation may be placed into statutory management in two situations:

- (a). Where the corporation is or may be operating 'fraudulently or recklessly'; or
- (b). Where the interests of the parties or of the public cannot be adequately protected under any of the Companies Acts legislation in force in New Zealand currently or in any other lawful way.

(i). The justification of a 'statutory management' regime in New Zealand:

New Zealand should aim to enact and have in place more effective machinery to facilitate the recovery of economic units which are financially distressed but are capable of salvage. The legislation or any modifications made to it should aim to avoid wastage of resources which could possibly result from a premature liquidation or receivership. A statutory management regime may be justified in some situations and I believe the CIMA 1989 is justified by the scale and specialised, defined type of client it deals with⁷⁵. The CIMA 1989 regime is simply put, justified by economics of scale. The fact that it does provide an alternative to normal insolvency procedures in the case of large and complex groups of companies is justified by the fact that the investigations required to delve into such complex intertwined company records and the fact high level white collar crime and fraud involving potentially millions and billions of dollars justifies a higher level insolvency regime. A related issue here is the period of the moratorium which at the moment is indefinite. Several submissions voiced in response to the Securities Commissions paper "The Corporations (Investigation & Management) Act 1989: A Discussion Paper", suggested a more conservative and fixed term

interest and resolve the difficulties of the corporation as far as practicable, and preserve the business or undertaking of the corporation as far as practicable.

⁷⁵ For example, such a regime that is justified is the regime included in the Reserve Bank of New Zealand Act 1989, where the objective is to protect the financial system itself.

period. Prior to the Equitcorp, Richmond Smart and Chase appointments the use of the statutory management regime was inevitably associated with issues of fraud or misconduct which could not be adequately dealt with by normal legal processes due to reasons of size and complexity. For the same reasons that justified the earliest corporate rescue act, the need to monitor large, complex, powerful, well resourced, corporations based upon economics of scale and size warrant the Securities Commission recommendations being heeded to and the statutory management regime being left intact and unmodified throughout the near future reforms.

8. New Zealand's current position:

It is very clear that Part XIV of the Companies Act 1993 which provides for creditor compromise arrangements, should in essence be retained in the future reforms based upon their informality, cost and ease of implementation. Our legislators have done a fine job in enacting Part XIV on almost identical terms to its counterpart contained in section 425 of the UK Insolvency Act 1986. Part XIV has an obvious purpose to serve and should not be modified significantly in its effect. However I agree with the JIC that Part XIV can be modified in the sense of including or adding to that provision an option for an Voluntary Administration regime. It has been shown that statutory management is a justified high level regime that is heavily regulated and monitored and deals with vastly different scenarios than a voluntary administration scheme would.

9. Conclusion:

I agree with writer Paul Heath that New Zealand can accommodate and is ready to accommodate an additional corporate rescue mechanism, namely in the form of a voluntary administration system (given the recent proposals and discussions about adopting one). I agree with the Joint Insolvency Committee in their recommendations⁷⁶ that by modifying Part XIV and adopting the voluntary administration into that provision, they have struck the right balance between protecting the rights of secured creditors who may otherwise be subject to a moratorium (on the one hand) and the need for a moratorium to assess adequately whether rehabilitation and sale of a business as a going concern is a viable option on the other hand.

Is it safe to conclude that any form of rescue procedure would help to deal with the rescue or restructure of companies in difficulty. Our government should aim to use such a mechanism to regulate failure in order to improve the efficiency of capitalism, as a means of allocating the resources of society in a way that does not cause harm or hardship to the vulnerable members of society.

New Zealand should not commit itself to a Voluntary Administration regime until such time as the detail has been worked and the Ministry of Commerce has been able to carry out an analytical appraisal of draft legislation. At that stage it will be possible to assess whether what the Joint Insolvency Committee has proposed on a conceptual level will in fact improve available remedies.

⁷⁶ The JIC's findings were also consistent with existing company laws and basic principles of insolvency law generally in New Zealand.

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