

New Zealand

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New Zealand company law was originally based on the English model, with a bias towards protecting creditor interests through management of the business and orderly realisation of assets. The reformed Companies Act and new Receiverships Act – both introduced in 1993 – drew more on Australian and Canadian law, but still emphasised protection of creditors rather than rehabilitation of the debtor.

Corporate insolvencies which typically occur in New Zealand include:

- receiverships, where a secured creditor acts to recover debt;
- interim or full liquidations by order of the court;
- liquidations arising from a resolution of the shareholders or board of directors, or following an event specified in the company's constitution;
- compromises; and
- statutory managements.

The following legislation governs these corporate insolvency administrations:

- the Receiverships Act 1993;
- the Companies Act 1993;
- the Companies Act 1993 Liquidation Regulations 1994;
- the Incorporated Societies Act 1908 and amendments; and
- the Corporations (Investigation and Management) Act 1989.

In line with international trends, however, there is an increasing focus on turnaround management and restructuring of distressed companies, and this change of approach is reflected in the proposed Insolvency Law Reform Bill currently before the New Zealand Parliament.

The Insolvency Law Reform Bill proposes:

- adjustment of the priority payment regime in liquidations;
- a voluntary administration regime for formal business rehabilitation based on the Australian model;
- provisions to encourage creditors to take a more proactive approach to protect assets of a financially distressed debtor;
- amendment of the present voidable transactions or 'clawback' regime;
- solutions for perceived issues arising from the use of 'phoenix' companies; and
- implementation of the United Nations Commission on International Trade Law Model Law on Cross-Border Insolvency to facilitate recognition of a single insolvency procedure.

1. Legal framework and the effectiveness of court processes/legal remedies

1.1 Describe the nature and effectiveness of the following:

(a) Debt recovery remedies where the creditor has no security

The following debt recovery remedies are available to unsecured creditors:

- The creditor may issue proceedings in the district court or High Court (depending on the value of its claim) and obtain judgment.
- The creditor may issue a statutory demand which, if not satisfied, provides a basis for an application to liquidate the company.
- In some circumstances, the creditor can claim a lien over property of the debtor, entitling the creditor to retain the property until payment is received.

Prior to obtaining judgment in the district court or High Court, it may be possible for an unsecured creditor to obtain:

- a Mareva injunction preventing the debtor from disposing of, dissipating or removing assets from New Zealand until the dispute which is the subject of the litigation is determined;
- a preservation of property order requiring the detention or preservation of the property that is the subject of the litigation; or
- a pre-judgment charging order preventing the debtor's property from being dealt with.

Once judgment has been obtained in the district court or the High Court, it may be enforced by:

- a charging order preventing the debtor's property from being dealt with;
- a writ of sale enabling the sale of the debtor's property; or
- a garnishee order entitling the creditor to receive payment of an amount owing to the debtor by a third party.

(b) The enforcement of security

A range of options are available to secured creditors to enforce their security. A secured creditor may:

- seize assets charged by its security;
- sell those assets; or
- appoint a receiver in respect of those assets.

The power to seize and sell property subject to

security is provided for by Section 109 of the Personal Property Securities Act 1999. This allows a secured party to realise assets subject to a security interest even where the security agreement itself may not provide for a contractual right to seize and sell.

A receiver may be appointed to protect rights or to collect and protect property over which security has been given. The law relating to receivers is largely governed by the Receiverships Act 1993. The power to appoint a receiver is a contractual right. It cannot be exercised until the occurrence of a specified event set out in the relevant security agreement. The receiver has the power to:

- manage the affairs of the company;
- issue proceedings in the name of the company (except if the company is also in liquidation) in order to collect and sell its property;
- carry on its business; and
- generally act as the company's agent.

Appointment of a receiver can be a particularly useful way in which to realise the going-concern value of a business. However, the costs of receivership can be significant, and these must be paid before any secured creditor receives payment on the realisation of assets subject to the security.

(c) Corporate bankruptcy/liquidation processes

A creditor may apply to court to liquidate a debtor company. The High Court retains discretion as to whether to make an order liquidating the company but generally, if it is established that the company is insolvent, a liquidation order will be made. A company can be liquidated if it is unable to pay its debts as they become due in the normal course of business.

A company may put itself into liquidation if the shareholders pass a special resolution to this effect or if the board of directors passes a resolution on the occurrence of an event specified in the company's constitution.

(d) Formal corporate rescue processes

A formal corporate rescue process is provided by Parts XIV and XV of the Companies Act 1993.

Pursuant to Part XIV, a debtor company may enter into a compromise with its creditors. The compromise may provide for:

- cancellation of all or part of a debt;
- variation of the rights of creditors or the terms

of a debt; or

- amendment of the company's constitution to affect the company's liability to pay the debt.

A compromise proposal may be made by:

- the board of directors of the debtor;
- a receiver appointed in relation to the whole or substantially the whole of the assets in the undertaking of the debtor;
- a liquidator of the debtor; or
- any creditor or shareholder of the debtor, with the leave of the court.

Notice of any proposal must be given to each known creditor. Approval of a compromise requires that a majority in number and 75 per cent in value of each class of creditors vote in its favour. Once approved, the compromise is binding on the debtor and on each creditor that received notice of the proposal.

A debtor may also enter into a compromise with its creditors pursuant to Part XV of the act. Under Part XV it is not necessary to obtain the approval of a majority in number and 75 per cent in value of each class of creditors. Pursuant to Part XV, the court has the ability to impose a compromise on creditors that would not have been possible under Part XIV, provided that an "intelligent and honest businessperson" might approve of the compromise.

There are proposals for the introduction of a voluntary administration regime similar to that in Australia. The legislation to achieve this is currently in draft form.

(e) Informal corporate rescue processes

Informal corporate rescue processes are a matter of negotiation between the debtor and its creditors.

1.2 What are the formal processes to effect a liquidation of the company's assets?

The appointment of a liquidator can be effected by one of the following three methods:

- by special resolution of the shareholders, irrespective of the company's constitution;
- by resolution of the board of directors, upon the occurrence of an event specified in the company's constitution; or
- by order of the High Court on the application of the debtor, a director, a shareholder, a creditor or the registrar of companies.

1.3 What is the effect on debt collection and the enforcement of security of:

(a) An adjudication of corporate bankruptcy/liquidation?

Without the liquidator's agreement or an order of the High Court:

- no legal proceedings may be commenced or continued against the debtor in relation to its property; and
- no right or remedy over or against the debtor's property may be exercised or enforced.

Further, a creditor is not entitled to retain the benefit of any execution process against the debtor's property unless the execution process is completed before the commencement of liquidation.

However, a secured creditor may enforce its security over the charged property, except where it has surrendered its security.

(b) The commencement of a formal corporate rescue process?

An approved compromise is binding on all creditors (both secured and unsecured) whose class confirmed by a majority vote in its favour, except where the creditor failed to receive notice of the compromise or the court orders otherwise. However, no class of creditors is bound prior to approval of the compromise.

(c) The initiation of an informal corporate rescue process?

The impact on the debt recovery process will be regulated by the terms of the contract where an informal corporate rescue process arises through contractual agreement between the debtor and its creditors.

(d) The initiation of an insolvency or insolvency-related process under any special legislation?

The appointment of a statutory manager under the provisions of the Corporations Investigation and Management Act imposes a moratorium on all proceedings, enforcement of judgments, liquidation applications, exercise of a security holder's powers, distraint and rights of set-off.

1.4 Are insolvency procedures involving a corporation incorporated in your jurisdiction recognised if they are started in another jurisdiction?

The circumstances in which insolvency procedures commenced in another jurisdiction will be recognised in New Zealand are not clearly defined. In principle, the courts have indicated that they wish to cooperate with insolvency procedures invoked in similar jurisdictions, but not where to do so would cause substantial prejudice to New Zealand creditors of the company.

The court also retains jurisdiction to liquidate the New Zealand assets of an overseas company notwithstanding any liquidation processes commenced in another jurisdiction.

1.5 In what circumstances would the directors or officers of a company in financial difficulties face potential personal liability for continuing to trade? In practice, are any such provisions actually enforced?

Directors may be liable for continued trading where they have breached their duties by allowing the company to continue trading. Directors are under a duty:

- to act in good faith and in what they believe to be the best interests of the company (Section 131 of the Companies Act);
- to exercise their powers for a proper purpose (Section 133 of the Companies Act);
- not to act or agree to the company acting in contravention of the Companies Act or the company's constitution (Section 134 of the Companies Act);
- not to:
 - agree to the company's business being carried on in a manner likely to create a sufficient risk of serious loss to the company's creditors; or
 - cause or allow the company's business to be carried on in a manner likely to create a substantial risk of serious loss to the company's creditors (Section 135 of the Companies Act);
- not to incur an obligation unless the director believes on reasonable grounds at the time that the company will be able to perform the obligation when required (Section 136 of the Companies Act); and
- to exercise the care, diligence and skill that a reasonable director would exercise in the circumstances (Section 137 of the Companies Act).

While these provisions have historically been used sparingly, the number of claims brought against directors for breach of duties has increased recently.

2. What are the advantages and disadvantages of triggering a formal procedure?

The advantages of triggering a formal procedure include the following:

- The debtor's assets are protected by an insolvency professional who is obliged to act in the interests of creditors.
- Unsecured claims are frozen as of the date of liquidation.
- A liquidator can investigate the affairs of the debtor and the reasons for its failure, and can bring claims in respect of any breaches of duty owed to the debtor.

The disadvantages of triggering a formal procedure include the following:

- The expense of the liquidation may mean that the costs incurred by the liquidator exceed any recoveries made.
- Once a company has been placed into liquidation, there is virtually no prospect that it will trade its way out of its financial difficulties.
- The voidable transaction provisions of the Companies Act are triggered, which may result in any payments made prior to liquidation being set aside.

3. What are the practical options for out-of-court restructuring?

Out-of-court restructuring can be effected through either one or a combination of the following options:

- restructuring of existing debt;
- sale of assets;
- sale and/or closure of business divisions;
- formal compromise with creditors;
- forgiveness of debt;
- capitalisation of debt;
- introduction of new equity or venture capital; or
- provision of additional security or guarantees/pledges for existing debts.

4. What is the effect on the management of a company of:

4.1 An adjudication of corporate bankruptcy/liquidation?

Upon appointment, the liquidator takes custody and control of the debtor's assets. Although the directors remain in office, their powers, functions and duties effectively cease.

4.2 The commencement of a formal corporate rescue process?

The extent to which management's rights are affected by a formal corporate rescue process will be determined by the terms of any compromise entered into. These may require the alteration of the management structure and the appointment of an external party to implement or supervise the compromise.

4.3 The initiation of an informal corporate rescue process?

In an informal corporate rescue process, the impact on the debtor's management will depend on the terms agreed between the debtor and its creditors.

4.4 The initiation of an insolvency or insolvency-related process under any special legislation?

Upon the appointment of a statutory manager under the Corporations Investigation and Management Act, all management powers, duties and responsibilities vest in the statutory manager. The directors' powers are suspended and they have no further involvement in the corporation's management, except where permitted by the statutory manager.

5. Role of key players involved in the restructuring and insolvency process

5.1 Who is responsible for the 'case management' control and administration of a corporate bankruptcy/ liquidation, a formal rescue or an informal rescue?

Responsibility for case management rests with the receiver in a receivership and the liquidator in a liquidation.

Case management in formal and informal rescues rests with one or more of the following:

- a compromise manager in an approved compromise;
- existing directors and management;
- the banking syndicate or lead bank;
- an independent third party, such as an insolvency practitioner; and
- a committee comprising members from the above.

5.2 Who is responsible for the 'case management' control and administration of a case of corporate insolvency under any special legislation?

The statutory manager(s) appointed under the Corporations Investigation and Management Act is responsible for case management in a statutory management.

5.3 Who is responsible for preparing the restructuring plan in a formal or informal rescue?

In a formal or informal rescue, the restructuring plan is prepared by those parties who are responsible for case management (see section 5.1).

5.4 Who is responsible for preparing the restructuring plan in a case of corporate insolvency under any special legislation?

The statutory manager(s) appointed under the Corporations Investigation and Management Act is responsible for preparing the restructuring plan (see section 5.2).

6. What financial information is available to creditors in a corporate bankruptcy/liquidation, a formal rescue and an informal rescue?

Upon liquidation, the liquidator must send to the registrar of companies and every known creditor notice of his appointment and a report containing, among other things, a statement of the debtor's affairs and proposals for the conduct of the liquidation. However, this report, and the subsequent six-monthly reports that must be provided thereafter, are not required where the anticipated distribution to unsecured creditors is unlikely to exceed 20 cents in the dollar.

Unless the court orders otherwise, the accounts and records of a company in liquidation may be inspected only by a liquidation committee (made up of representative creditors and/or shareholders), if one has been established.

A receiver must file with the registrar of

companies a first report within two months of his appointment and subsequent reports every six months thereafter. Copies must also be sent to the secured creditor which appointed the receiver and any other creditor that requests a copy. The receiver's report must include:

- the assets comprising the property in receivership;
- particulars of the debts and liabilities to be satisfied from those assets;
- amounts owed to the preferential creditors and to the secured creditor that appointed the receiver; and
- amounts available to other creditors.

Other information may be provided to creditors from time to time as the liquidator or receiver deems necessary, but will not necessarily be made publicly available.

7. Financial issues

7.1 What are the main areas from which funding is generally utilised by companies undertaking either formal or informal restructuring?

Funding may be obtained:

- through refinancing either with existing financiers or with another lending institution. Such funding is usually secured by first-ranking specific or general security over the company's assets, with additional collateral, if required, provided by way of personal guarantees of directors and/or shareholders;
- from trade creditors in certain circumstances where new funding is given in priority over existing debt;
- from directors and/or shareholders providing additional funding from external sources to mitigate potential personal guarantee liabilities; or
- through an external third-party equity investor which provides funds in exchange for a stake in the company.

Funding by way of debt or equity may be available from central or local government where the company subject to the rescue has a strategic place in New Zealand's economy or infrastructure.

7.2 In what order are creditors paid in a corporate bankruptcy/liquidation?

In a liquidation, a secured creditor with a valid security over assets of the company may enforce its security over the charged assets provided it has not surrendered its security. Otherwise, the liquidator applies the assets in the following order:

- payment of the liquidator's costs and expenses incurred in administering the liquidation;
- payment of employee claims for unpaid wages, holiday pay and redundancy payments payable under an employment contract to a maximum of NZ\$15,000 per employee;
- payment of certain unpaid taxes (excluding income tax);
- payment of creditors with security over accounts receivable and/or inventory; and
- from any remaining assets, *pro rata* payment of all other unsecured claims ranking equally.

7.3 Are there any legal provisions that might operate to invalidate the creation of security, the disposal of an asset or the payment of a creditor by a company in financial difficulties?

Upon the appointment of a liquidator (or, in the case of a court-appointed liquidator, the date on which an application to liquidate the debtor is made to the court), the voidable transaction provisions of the Companies Act are triggered. A transaction made by a company other than in the ordinary course of business at a time when the company was unable to pay its due debts is voidable if:

- it was entered into within a specified period; and
- it enabled another entity to receive more towards satisfaction of a debt than it would have received in the company's liquidation.

Similarly, charges over any property of the company are voidable if they were executed during the specified period at a time when the company was unable to pay its due debts immediately after the execution of the charge, except where:

- the security was given in substitution for earlier security;
- the charge secured money advanced, the value of property supplied or other valuable consideration given in good faith at the same time or after the charge was executed; or
- in the case of a charge securing the purchase price of property, the security was given within

30 days of the sale of the property taking place.

7.4 What is the position of both unsecured and secured creditors that vote against, do not agree with or do not consent to either a formal or an informal rescue plan?

A compromise approved by creditors or a class of creditors (including secured creditors) is binding on all creditors or all creditors of that class, provided that those creditors were given notice of the compromise. Secured creditors are not precluded from exercising their powers under their security unless they agree to be bound by the compromise.

A creditor can apply to the court for an order that it is not bound by the compromise if:

- insufficient notice of the meeting was given;
- there was some other procedural irregularity in obtaining approval; or
- the compromise is unduly prejudicial to the creditor or to the class of creditors.

7.5 What actions can creditors take if they are not satisfied with the conduct of either a formal rescue procedure or a corporate bankruptcy/liquidation?

Creditors of a company in liquidation have recourse to the High Court, which has the power to make orders confirming, reversing or modifying the acts of a liquidator or compelling the liquidator to comply with the relevant duty or face removal. Similar rights exist in relation to receivers.

8. General

8.1 Can the insolvency regime be described as systematic and efficient for:

(a) The liquidation of businesses incapable of being restructured?

Yes.

(b) The restructuring of debt?

The formal procedures are clumsy and rarely used. A new proposal to introduce a voluntary administration regime should make the procedure more systematic and efficient.

8.2 What are the biggest legal and non-legal impediments to the systematic and efficient liquidation of businesses and restructuring of debt?

The current legislation has no automatic stay provision while a restructuring attempt is put in place. This allows creditors to put a restructuring proposal at risk by taking enforcement remedies before it is implemented.

8.3 Has the insolvency regime been reformed in the last two years? If so:

(a) What are the reforms?

In the past two years the Companies Amendment Act 2004 has been passed, amending Section 104 of the Insolvency Act 1967 in relation to redundancy payments and increasing the cap on employee claims for unpaid wages and the like. The reform has been implemented so as to provide for the preferential payment of monies owing to employees in respect of redundancy payments, and to increase the cap on preferential payments to employees from NZ\$6,000 to NZ\$15,000.

(b) Are the reforms being implemented so as to facilitate the systematic and efficient handling of corporate insolvency cases?

Significant reforms proposed by the Insolvency Law Reform Bill are currently in draft form but have not yet been passed (see the introductory section).

8.4 Are there any other legal or non-legal changes in the last two years that have impacted on the operation of the insolvency law regime?

While corporate legislation over the last two years has not changed, the operation of the insolvency law regime has been affected by an increase in legal proceedings brought against directors for failing to maintain proper accounting standards, breaching corporate governance responsibilities or, more rarely, committing fraudulent acts. Insolvency practitioners are now looking more closely at recovery from directors who have breached their fiduciary duties to the detriment of the company and its creditors.

8.5 Is statistical information on insolvency cases and corporate insolvency published? If so, how? Is it easily and freely accessible?

Very little statistical information on insolvency cases is available in New Zealand.

8.6 What is the most urgent reform required to facilitate the systematic and efficient handling of corporate insolvency cases (formal and informal)?

The most urgent reform required to facilitate the systematic and efficient handling of corporate insolvency cases is the introduction of a voluntary administration regime, as set out in section 8.1.