



37/50 = 74%

SUMMATIVE (FORMAL) ASSESSMENT: MODULE 8F

RESIT ASSESSMENT: SEPTEMBER 2023

NEW ZEALAND

This is the summative (formal) assessment ***for*** Module 8F ***of this course and is compulsory for all candidates who*** selected this module as one of their elective modules.

The mark awarded for this assessment will determine your final mark for Module 8F. ***In order to pass this module, you need to obtain a mark of 50% or more for this assessment.***

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

- 1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.**
- 2. All assessments must be submitted electronically in Microsoft Word format, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters - please do not change the document settings in any way. DO NOT submit your assessment in PDF format as it will be returned to you unmarked.**
- 3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).**
- 4. You must save this document using the following format: [studentID.assessment8F]. An example would be something along the following lines: 202223-336.assessment8F. Please also include the filename as a footer to each page of the assessment (this has been pre-populated for you, merely replace the words "studentnumber" with the student number allocated to you). Do not include your name or any other identifying words in your file name. Assessments that do not comply with this instruction will be returned to candidates unmarked.**
- 5. The final submission date for this assessment is 21 September 2023. Please provide the completed assessment back to Sanrie Lawrenson via email at Sanrie.Lawrenson@insol.org by no later than 23:00 (11 pm) GMT on 21 September 2023. No submissions can be made after this time, no matter the circumstances.**
- 6. When submitting your assessment you will be required to confirm / certify via email that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**

ANSWER ALL THE QUESTIONS

QUESTION 1 (multiple-choice questions) [10 marks in total] **6 marks**

Questions 1.1. - 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow. Select only ONE answer. Candidates who select more than one answer will receive no mark for that specific question.**

Question 1.1

Select the incorrect answer:

A voluntary administrator may be appointed by:

(a) A secured creditor.

(b) A liquidator.

(c) The Board of Directors.

(d) A receiver.

Question 1.2

Select the correct answer:

A liquidator in New Zealand is supervised by:

(a) The directors.

(b) The Court.

(c) The Ministry of Business, Innovation and Employment.

(d) The shareholders of the company.

Question 1.3

Select the correct answer:

Receivers in New Zealand:

- (a) **Are the agent of the secured creditor.**
- (b) *Act in the interests of unsecured creditors.*
- (c) *Have powers granted by the secured creditor.*
- (d) **Are governed by the Receiverships Act 1993.**

Question 1.4

Select the correct answer:

A secured creditor in New Zealand:

- (a) *is not subject to the voluntary administration regime.*
- (b) *is granted rights under the Personal Property Securities Act 1999.*
- (c) **must perfect its interest under the Personal Property Securities Act to maintain priority in relation to its security interest.**
- (d) *has priority over all other creditors of the company.*

Question 1.5

Select the correct answer:

Company A goes into liquidation. Which of these claims has first priority?

- (a) *PAYE owed to the Inland Revenue.*
- (b) *Employee claims.*
- (c) **The Liquidator's costs and expenses.**
- (d) *Costs of the creditor who applied to put the company into liquidation.*

Question 1.6

Select the correct answer:

- (a) **A security interest is created by a financing statement under the Personal Property Securities Act 1999.**
- (b) *Failure to perfect a security interest renders a security interest invalid.*

(c) An unperfected security interest is not enforceable against the Official Assignee or liquidator.

(d) Priority between competing perfected interests is governed by time of registration.

Question 1.7

Select the incorrect answer:

(a) A debt repayment order is available to debtors with total debts of under NZD\$50,000.

(b) Bankruptcy in New Zealand can be voluntary or forcible.

(c) A bankruptcy remains in place for three years from the date a person is adjudicated bankrupt.

(d) A bankruptcy is searchable for seven years after the conclusion of a bankruptcy

Question 1.8

Select the incorrect answer:

The liquidation regime in New Zealand:

(a) is governed by the Companies Act 1993.

(b) is a collective process.

(c) can be voluntary or involuntary.

(d) allows a secured creditor to be paid in priority to unsecured creditors.

Question 1.9

Select the incorrect answer:

Secured creditors in New Zealand:

(a) have powers conferred by the security agreement granted by the debtor company.

(b) stand outside the liquidation of a company.

(c) may be required to make an election to enforce their rights under the liquidation regime.

(d) **have no rights in the administration of a company.**

Question 1.10

Select the correct answer:

A monetary debt judgment obtained from the High Court in Singapore may be enforced in New Zealand under the:

(a) **Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil or Commercial Matters.**

(b) **Reciprocal Enforcement of Judgments Act 1934.**

(c) **Trans-Tasman Proceedings Act 2010.**

(d) **Common law.**

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 5 marks]

(a) **Name three types of actions an Official Assignee (OA) or liquidator may take to recover assets for the benefit of unsecured creditors. 3 marks**

(b) **Give two policy reasons for these powers being conferred on the OA and / or liquidators. 2 marks**

Answer:

The Insolvency Act 1967 (the Act) governs the appointment of Official Assignees (OA) and liquidators and sets out their powers and way they are to administer bankrupt estates. The three types of action which they may take for the benefit of unsecured creditors are to:

1. Apply to a court having jurisdiction to set aside or cancel an assortment of “insolvent transactions”, including voidable transactions, transactions at undervalue or for inadequate or excessive consideration, and insolvent gifts (that is, transactions which favour a particular creditor or class of creditors or amount to a lawful diversion of company assets to a third party, to the detriment of the general body of creditors, all being insolvent transactions defined in the Act.)
2. Institute claims which vest in the company, including claims against directors for breach of duty and other fiduciary responsibilities which directors are required to uphold.

3. Lodge a claim under the Property Law Act 2007 in instances where a disposition of property was carried out to defeat creditors' interests.

Two policy reasons for these powers being conferred to the OA / liquidator are:

1. To ensure that all creditors of classes are treated equally within an orderly, collective, administrative process, and thus maintain the principle of *pari passu* and to ensure that creditors, already prejudiced by the failure of the insolvent company (or individual) in that they will be unable to fully recover debts owed to them, can nonetheless recover as much as is possible alongside their co-debtors of a particular class without some creditors being favoured above others.
2. To enable the OA / liquidator, when administering an insolvent estate, to conduct a thorough investigation of the affairs of the estate, and thereafter take steps to expand the pool of assets capable being realized for distribution to the creditors. This is done by using effective means to recover assets as may have been disposed of in a manner and at a time deemed unacceptable by the Act, and to claim damages from those may have been responsible for, or complicity in, mismanaging the bankrupt estate. Not only does this ensure a measure of fairness and equity in the distribution of the bankrupt estate's assets, but also has the effect of discouraging soon to be bankrupt companies, their controllers, and greedy and or powerful creditors from acting to the detriment of the general body of creditors, and to also hold such persons to account.

Question 2.2 [maximum 3 marks] **0 marks**

Efficiency in administration of a liquidation is important to maximise recovery for creditors in a liquidation. Name three ways this policy is given effect to, under the recovery process in New Zealand.

Answer:

1. By creating a specialist jurisdiction in the High Court with dedicated court lists of insolvency matters which are dealt with by associated judges who focus primarily on company and insolvency matters.
2. By implementing the UNCITRAL Model Law with effect from July 2008, enabling bankruptcy proceedings initiated elsewhere to be extended to recovery of New Zealand based assets.
3. A liquidator can cancel irregular transactions in a very short period of time by giving the recipient a limited time of 20 working days to respond and if no objection is made

within that time the transaction is automatically set aside and the assets can be recovered.

4. The liquidator may bring claims in respect of voidable transactions using a simplified summary process under Part 19 of the High Court Rules. Evidence is by way of affidavit and no detailed pleading need be filed.

In terms of the recovery process

- ***Presumption of insolvency in six month prior to liquidation in voidable claims and charges - removes issues around demonstrating insolvency for liquidators.***
- ***Most recovery actions are summary court processes - removal of need for discovery etc to facilitate quicker resolution of liquidation actions.***
- ***Process of receiving creditor claims - enables a liquidator to make decisions to accept and/or reject creditor claims without protracted court process.***
- ***Court supervision of liquidator***
- ***Summary section under Companies Act 1993 (s 301) to bring claims for mismanagement etc.***

Question 2.3 [maximum 2 marks] **2 marks**

Name the relevant legislation which might be utilised when assessing enforcement of an overseas Court order in New Zealand. What factor would you first consider, when deciding which option will most likely apply?

Answer

There are three pieces of legislation available:

1. The Reciprocal Enforcement of Judgments Act, 1934
2. The Enforcement of Commonwealth Judgments Under Senior Courts Act, 2016
3. The Trans-Tasman Proceedings Act, 2010.

The first factor is to consider the *forum* in which the foreign judgment was obtained in the sense of both the country where the judgment was obtained, and whether it is a judgment of a recognized court of law.

QUESTION 3 (essay-type questions) [15 marks in total] **10 marks**

What are the different insolvency processes available in New Zealand to corporate entities? Which of these are not collective processes?

Of these processes, why are some more processes more popular than others? Discuss potential reasons for this, having regard to New Zealand's commercial context and the

procedural requirements of each of the processes. What factors might influence what advice you might provide to a board of directors about options going forward, if a company approached you showing signs of potential distress?

Answer:

The different insolvency processes available in New Zealand are:

1. Receiverships
2. Liquidations
3. Voluntary Administration
4. Creditors Compromise
5. Business debt hibernation
6. Statutory Management

Bankruptcy

Receivership is not a collective process.

As a general statement, most companies in New Zealand are small to medium enterprises, many of which are limited liability companies. Money or the lack thereof is therefore an important consideration when it comes to paying fees and being financially able to wait for process to reach their end. Articles and textbooks suggest that factors that might play a role in determining preferences include the desire for fairness, efficiency, curtailing costs and delays, timeliness, equal treatment of creditors as well as the need to time the insolvency process with a view to achieving the highest prices for the assets. The procedural requirements for the different processes vary according to the reason for needing to launch insolvency steps and the result required.

I shall now address the six processes independently.

Receivership

Receivership starts with the appointment of a receiver under the terms of a security agreement to mainly realize secured assets to the benefit of a secured creditor(s) (security holder) who appointed the receiver. The process is governed by the Receiverships Act 1993, and it is not a collective process.

Receivers are appointed either by the High Court, in which case the receiver is supervised by the court, is not answerable to the creditors and the debtor (unless ordered by the court), must remain impartial and acts on the directions issued by the court. However, most receivers in

New Zealand are appointment privately by secured a creditor(s) in terms of a contractual agreement with the debtor which gives the creditor that right.

One drawback is that receivers need not be particularly qualified, and the regime is rather that those disqualified may not act, although even then with exceptions. The quality of receivers can therefore cause a lack of confidence in the system.

The rights of the receiver are both statutory, per the receivership Act, and contractual, while receivers are not able to disclaim contracts they do have the power to terminate employment agreements within 14 days otherwise they attract personal liability. They can also be liable for rent payments. It is understandable that person may be reluctant to take on such appointments, and when they do, act most conservatively in an effort not to attract personal liability. Largely, they tend to “obey” the wishes of the secured creditor and struggle to find the space to act impartially.

In summary, receivers are largely of little tangible assistance to the debtor, its board, or creditors, save for secured creditors. The only feature of receivership that a board of directors may find attractive is that the board remains in office and control of the company and its assets while the receivership takes place. But it is doubtful that this is a redeeming feature for most boards. Accordingly, I would not advise a board to actively support or encourage the appointment of a receiver.

Liquidations

A liquidator is appointed to wind up the affairs of a company. The principal duty of a liquidator lies in taking possession of, protecting, realizing, and distributing the distressed company’s assets (or their proceeds) to its creditors according to their class status. The liquidator then distributes any remaining surplus to the company’s shareholders or whomever else is entitled to such surplus per the company’s founding documents.

Part 16 of the Companies Act 1993, read with the Insolvency Act, govern the appointment and powers of the liquidator. A liquidator can be appointed by the High Court or by special resolution of shareholders or by a resolution of directors when directly permitted by the company’s founding documents. Moreover, the creditors can appoint a liquidator by resolution at a ‘watershed’ meeting.

Once a company is in liquidation, an unsecured creditor cannot, without the permission of either the court or the liquidator, start or continue any legal proceedings against the company

or its property, or start or continue to enforce rights against the property of the company. **On the other hand**, liquidation does not prevent secured creditors from exercising their rights, although certain preferential creditors will still be paid out from the proceeds of inventory and accounts receivable.

A liquidator is expected to investigate the affairs of the company (to the extent that funding allows) and may bring claims, sue directors, apply to cancel insolvent transactions and claw back monies irregularly paid from the company with the purpose of increasing the pool of company funds from which to pay creditors.

For purposes of transparency, a liquidator must give regular reports to every known creditor, shareholder, and to the Registrar of Companies. A liquidation is complete when the liquidator sends a final report and various other documents to all creditors, shareholders and the Registrar of Companies.

Lastly, a liquidation process need not end with the total destruction the company. Throughout the process the liquidator shall be open to receiving compromise and other proposals which may either result in the revival of the company or its resurrecting in an altered, often more streamlined form.

When advising a board, the question of whether to seek a liquidation is heavily dependent of the true financial state of the company and its ability to continue to trade under solvent circumstances. Boards are often concerned with their legacy and thus boards often seek advice in business rescue type options. However, board members with an understanding of their fiduciary duties, and the consequences of non-compliance, are normally adverse to the risk of being held personally liable for the debts of the company should the decision to place the company in liquidation be postponed. Thus, where the prospects of financial recovery are bleak, a board will be persuaded by the notion of placing the company in liquidation albeit that it means they have to immediately give up control of their company and place it in the hands of a liquidator.

Voluntary administration

Voluntary administration entails the appointment of an administrator to assess a company's affairs and options going forward, often in the hope that a way can be found to keep the company in business. Voluntary administration is governed by Part 15A of the Companies Act 1993 and primary objectives are to provide for the affairs of an insolvent company, or one that

may become insolvent, to be administered in a way that maximizes the chances of the company, or at least parts of it, continuing in existence; or, if that is not possible to achieve, then to operate the company for a limited time with the aim of achieving better financial returns for the creditors than they will receive from an immediate liquidation.

Administrators may be appointed by the Court, a liquidator (if the company is in liquidation), the company's directors, or a secured creditor holding a charge over the whole, or substantially the whole, of the company's property. Appointment of an administrator to a company which is already in liquidation will suspend the liquidation as she tries to find a way to avoid the complete destruction of the company. On the other hand, an appointment of an administrator does not have the effect of removing a receiver from office.

An appointment of an administrator to a company not yet in liquidation immediately causes a moratorium to come into effect which prevents anyone from bringing or continuing proceedings against the company or enforcement processes in relation to the company's property without the administrator's consent or court permission (with some exceptions). This is meant to give the company breathing space to allow the administrator time to assess whether the company should enter into a deed of company arrangement (DOCA), be placed into liquidation, or come out of administration in which case the directors resume their roles.

When advising aboard on the options, this is often the most chosen one given that it provides the directors time to consider the future without being hounded by creditors seeking to enforce their rights. The introduction of an experienced administrator can assist the board in understanding their position viz-a-viz the real prospects of being able to continue in business either in the present form or in terms of a compromise or restructuring agreement (DOCA) negotiated with their creditors. However, there are instances where the dire state in which the company finds itself cannot be ignored and, in those cases, the board is advised to consider proceeding straight to liquidation.

Creditors Compromise

A creditor compromise is a further process under the Companies Act whereby a company may enter into an arrangement with its creditors. It can be attractive to creditors as it is often structured to include full and final settlement payments made over an extended period, or by using monies to which creditors in a liquidation would not be entitled to.

In practice, a proposal is made in a prescribed form for creditors to vote upon at a meeting and is effect and binding when the majority of creditors (50% by number and 75% by value) approve it. In the ordinary course, different classes of creditor must approve it separately.

The Court will not typically be involved unless called upon to persuade a reluctant creditor from wrecking the compromise. The compromise document must be formatted to include information such as details of the proposer, the terms of the compromise and reasons for it and the benefits for the creditors,

A board should be advised of various advantages to a compromise such as it may make raising capital or obtain new loans easier without historic debts being in place; a collective negotiation on the compromise is easier than many independent meetings; where a private restructuring process is preferred to one conducted in the glare of a VA or liquidation process; and, besides, creditors are likely to prefer to support a proposal if it means that they will receive a better financial result than they would in a liquidation or receivership. At the same time, the board can remain in control of the company knowing that the debt burden has been reduced significantly.

Business debt hibernation

During the COVID-19 pandemic, New Zealand introduced as so-called Business Debt Hibernation scheme to allow businesses to place their existing debts in 'hibernation' until they are able to resume trading at normal levels. It was available to companies, charitable trusts, partnerships and other entities. Sole traders were excluded as well as businesses that were not viable dur to insolvency issues prior to the pandemic. It was a once off scheme which could not be used more than once save if ordered otherwise by the Courts or the regulations permit companies to re-enter.

Eligibility standards included that directors must meet a threshold, while 50% of the creditors had to approve a proposal of a six-month moratorium on the enforcement of existing debts. Once the creditors and the Registrar of Companies were notified, the company enjoyed an immediate one month triggers an immediate one-month moratorium (during which trading cold continue) on the enforcement of debts pending approval of the proposal.

As an added incentive to creditors to agree to proposals, payments made to them during the duration of the scheme under a proposal would not be treated as voidable transactions should the company subsequently be placed in liquidation.

As the pandemic is over, the scheme is no longer available and thus it is not an option to be discussed with boards.

Statutory Management

Statutory management is a seldom used mechanism devised at the time to manage major corporate failures that were capable of causing systemic failure in the economy such as the collapse of a property-owning colossus and the subsequent sell-off of its properties into a weak market or an airline going out of business.

The primary purpose was to investigate the causes of the collapse so as to prevent further losses and contagion across the market(s). The creditors had little say in the process which was initiated by the Crown who also appointed the manager. While appointment of a manager triggered an absolute moratorium against enforcement of creditors rights, management was not allowed to play a role in the company unless expressly requested. Creditor participation is minimal.

The manager assumes the powers of the board and could carry on business, enter into compromises, sell assets notwithstanding security held by persons. The manager can access the courts for many purposes, not least to apply for the liquidation the company.

For obvious reasons, not least because of the exclusionary nature of the manager's powers leaving the board as mere spectators, it is unlikely that legal advisors would recommend to a board that they approach the Crown with a view to requesting that a statutory manager be appointed.

Advisory aspects / factors when showing signs of potential distress (such as are there secured creditors, duration of financial distress, guarantees by directors, would creditors support a rescue process, etc).

QUESTION 4 (fact-based application-type question) [15 marks in total]

Mr Strong is a director and shareholder of two New Zealand based companies. He returned to New Zealand from the UK, after spending a significant amount of his working career (some 35 years) travelling between the UK and New Zealand. His children remained in the UK when he returned to New Zealand. He has some accounts in the UK, but ceased to work rented while he lived in the UK. He has bank accounts in both the United Kingdom and New Zealand.

He worked in the UK for a number of years, but ceased to do so about a year after he returned to New Zealand. He sold his business in the UK and moved back to New Zealand. About two years later, proceedings were issued in the United Kingdom pursuant to a guarantee against Mr Strong. The creditor obtained judgment for £500,000 and subsequently petitioned for Mr Strong's bankruptcy in the United Kingdom. Ms Finder was appointed trustee of the bankrupt estate.

Mr Strong's entities, Weak Limited and Muscles Limited, were put into liquidation by a creditor after the issuing of a statutory demand. On investigation, the liquidators discovered:

- **In relation to Weak Limited, Mr Strong had paid himself a significant amount of money in satisfaction of his current account debt, in the two-year period prior to the liquidation.**
- **He transferred a property owned by Muscles Limited, to an entity of which he was also sole shareholder and director. The sale and purchase agreement shows a purchase price of \$500,000. The current valuation for the property is \$750,000. The transfer occurred in the year before liquidation.**
- **The balance sheet of both Weak Limited and Muscles Limited, show that both entities had negative equity for about a year prior to liquidation. The management accounts show the companies had significant creditors, most of which were outstanding for more than 90 days.**
- **Weak Limited and Muscles Limited owe \$1,000,000 to the NZ Bank (\$500,000 each). NZ Bank has security in its favour over all the assets of the companies, including accounts receivable and inventory. The security agreement includes provision for the NZ Bank to appoint a receiver. Mr Strong also provided a personal guarantee to NZ Bank in respect of the bank debt.**
- **There is approximately \$250,00 cash in bank across the two entities (\$125,000 in each company). There are debtors of about \$100,000 in each of the entities. There are some assets, but it is unclear how much they are worth. There are creditor claims of approximately \$1.5 million in each of the companies. The liquidators anticipate there will be a shortfall.**
- **NZ Bank has indicated it will pursue Mr Strong for any shortfall. Assume the bank will be successful in obtaining judgment against Mr Strong.**

Question 4.1 [maximum 8 marks] **8 marks**

You have been asked to advise the liquidators on steps it should take, to recover assets for the unsecured creditors.

Provide an opinion which addresses the following:

- ***Potential avenues of recovering assets, having regard to the elements that need to be established.***
- ***What factors a liquidator should have regard to before taking action, including whether the NZ Bank's position should be factored in.***

Answer:

Opinion

The liquidator seeks an opinion on the potential avenues to recover certain assets of Weak Limited (Weak) and Muscle Limited (Muscle), currently in liquidation, for the purpose of effecting an orderly distribution of all assets of Weak and Muscle to their unsecured creditors, and what factors she must have regard to when choosing a particular avenue.

Before addressing the avenues, the following facts should be emphasized.

1. Mr. Strong, in his capacity as director and shareholder, owned and controlled Weak and Muscle.
2. In the two years prior to liquidation of Weak, Mr. Strong paid himself "a significant amount of money" (from Weak) in satisfaction of his loan account debt.
3. In the year before liquidation of Muscle, Mr. Strong sold a property owned by Muscle for \$500 00-00, which is now valued at \$750 000-00.
4. Weak and Muscle had negativity equity for about a year prior to liquidation and, their management accounts show that they have numerous creditors outstanding for more than 90 days.
5. Weak and Muscle each owe New Zealand Bank \$5000 000-00. The Bank has a charge (or security) in its favour over all assets of the companies, including accounts receivable and inventory. Mr. Strong provided personal guarantees to the Bank which the Bank is likely to call up should there be a shortfall.
6. Against that background, the following avenues are open to the liquidator intent on recovering assets of Weak and Muscle. It will be assumed for purposes of this opinion that the liquidator has used her investigative powers to enquire into Weak and Muscle's affairs,

including transactions, and financial records to determine their financial position, assets, liabilities, and any potential wrongdoing.

7. In general, assets can be recovered as follows:

By setting aside insolvent transactions

7.1. By doing so, the liquidator, if successful, may recover the monies paid by Mr Strong to himself from Weak as the transaction has the hallmarks of a voidable transaction favouring a single, related party, creditor at a time when Weak was unable to pay its creditors.

7.2. By suing to set aside the transactions described in the instruction as “insolvent transactions”. In terms of section 195 (1) of the Insolvency Act, an insolvent transaction “is a transaction by the bankrupt [or insolvent company] that is entered into at a time when the bankrupt [or insolvent company] is unable to pay his or her due debts; and enables a creditor to receive more towards satisfaction of a debt by the bankrupt [or insolvent company] than that person would receive, or would be likely to receive, in the bankruptcy.

7.3. *The Insolvency Act defines “transaction”, as used in the term “insolvent transaction, to mean any of the following steps by the bankrupt (or insolvent company):*

- (a) conveying or transferring the bankrupt’s property:
- (b) giving a charge over the bankrupt’s property:
- (c) incurring an obligation:
- (d) undergoing an execution process:
- (e) paying money (including money paid in accordance with a judgment or an order of a court):
- (f) anything done or omitted to be done for the purpose of entering into the transaction or giving effect to it

7.4 The transaction must have taken place within a specified period before the companies were liquidated. The time periods are:

- a. The claw-back period has been restricted to six months for third party creditors.

- b. However, the claw-back period remains at two years for related party transactions.

The two-year time period is relevant to Mr. Strong as he is a related party.

7.5 The liquidator is obliged to first make demand in writing for repayment of the monies or property received from the impugned transaction, giving the recipient 20 court days to object, failing which the transaction is automatically cancelled. And the recipient objects, the liquidator must approach the court for an order setting aside the transaction.

By suing for return of, alternatively, compensation for the property sold by Muscle to Mr Strong's company.

8 Under section 348 of the Property Law Act (PLA), the High Court may set aside certain dispositions of property on application, "if satisfied that the applicant for the order has been prejudiced by a disposition of property to which this subpart applies".

9 Under section 347 of the Property Law Act, "the liquidator, if the debtor is a company in liquidation" (which it is), may apply for an order to recover the property or to be awarded compensation, that it sold to the entity owned and controlled by Mr Strong for \$5000 000-00, under section 348 of the Property Law Act.

10 To sustain such a claim, the liquidator must, in the application, "specify the disposition claimed to be prejudicial", and identify the property or compensation sought through the application." see section 347(2).

11 The application, together with a notice communicating the effect of [sections 348](#) and [349](#), must be served on the person in whose favour the disposition of property was made (i.e. the purchaser which is a company of which Mr Strong is a director and shareholder) and any other person (being Mr Strong) from whom property or compensation is sought through the application.

12 At the time that the property was sold, Muscle was experiencing liquidity problems and, it seems, may have been sold at a loss by Mr Strong to a related party (i.e. an entity owned and directed by Mr Strong whose was a director and shareholder of Muscle at the time). At the very least, the property has increased substantially in value and Muscle will have been prejudiced by the sale at an uneconomical price. Nevertheless, the section 348 application may lead to a substantial increase in the assets which the liquidator will be able to pool, thus increasing the likely pool available for distribution to the unsecured creditors.

Question 4.2 [maximum 7 marks]

Question 4.2.1 [maximum 4 marks] **4 marks**

Outside of recovering assets, are there other potential actions a liquidator could explore? What are they? What other information might you need to form a view as to whether or not there would be a viable claim?

1. The liquidator should consider bringing an action against Mr Strong in his (fiduciary) capacity as director of Weak and Muscle in terms of the New Zealand Companies Act (and possibly the common law), arising from breach of his fiduciary duties, for the payment of damages incurred by Weak and Muscle as a result of the payment of his loan account debt which resulted in Mr Strong's claim being favoured over that of other creditors at a time when Muscle was in financial difficulties.

2. These duties are described in the Companies Act as being:
 - a. Under section 133: "to act in the best interests of the company (which includes the interests of creditors when acting close to the time of insolvency) – aka a fiduciary duty of care: and

 - b. Under sections 135 and 136: "not to carry on business in a manner that is likely to create a substantial risk of serious loss to creditors, and not to agree to obligations without reasonable grounds for believing the company will be able to perform those obligations when due" – aka reckless trading

3. The liquidator must establish inter alia the liquidity of the companies and their ability to pay their creditors at the time of the breach, and if there were reasonable prospects of them subsequently returning to a state where they could pay their creditors, at the time Mr Strong effected the impugned transactions, and Mr Strong's knowledge of the companies' precarious position. Unfortunately, very recent case law from New Zealand suggests that, as such liability is personal to Mr Strong, he may not be questioned on whether he breached these duties during questioning by the liquidator under the Companies Act and Insolvency Act. This may hamper the liquidator in her efforts to acquire knowledge pertaining to the transaction.

4. The significance of the charge over the assets by New Zealand Bank.
5. Under non-insolvency circumstances, the charge would result in the Bank being a secured creditor and, as such, upon it calling up the loan, there would be little or no assets after realisation of the assets to pay the \$1 million owed by Weak and Muscle to the Bank. After liquidation, the charge continues to pose a threat to the unsecured creditors receiving any dividends.

6. However, in terms of section 198 of the Insolvency Act, “a charge over any property of a [liquidated company] may be cancelled on the [liquidator’s] initiative if—
 - a) the charge was given within 6 months immediately before the bankrupt’s adjudication; and
 - (b) immediately after the charge was given, the bankrupt was unable to pay his or her due debts.(2) A charge over any property of a bankrupt may be cancelled on the [liquidator’s] initiative if—
 - (a) the charge was given to a related party of the bankrupt within 2 years immediately before the bankrupt’s adjudication; and
 - (b) immediately after the charge was given, the bankrupt was unable to pay his or her due debts.”

7. It is unclear when, in this instance, the charge over the assets (by the way, property is given a very wide interpretation and would include movable assets) was given to New Zealand Bank, but if it was less than 6 months immediately before the companies’ adjudication (as insolvent); and that immediately after the charge was given the companies were unable to pay their due debts”, the liquidator would be entitled to seek an order cancelling the charge and thus freeing the companies’ assets for distribution to unsecured creditors.

8. But, be aware that, as expressed clearly in section 203, a charge agreed before specified period may not be cancelled in that: “ A charge given by the bankrupt under an agreement to give the charge—
 - (a) may not be cancelled under [section 198\(1\)](#) if the agreement to give the charge was made before the period of 6 months immediately before adjudication:
 - (b) may not be cancelled under [section 198\(2\)](#) if the agreement to give the charge was made before the period of 2 years immediately before adjudication.”

9. It is therefore important for the liquidator to establish the strength of the bank's security or charge, if it was undervalued or not and when it was given as, if it remains unchallenged, the Bank will be in a position to realise and retain the majority, if not all, the proceeds generated when the assets of Weak and Muscle are sold.

Question 4.2.2 [maximum 3 marks] 2 marks

You have been asked to advise Ms Finder as to potential avenues she could take, to recognise the UK bankruptcy in New Zealand.

What aspects of the Insolvency (Cross border) Act would be relevant to the advice? Do you think the bankruptcy would be recognised in New Zealand? Why or why not? How would the bankruptcy of Mr Strong in New Zealand affect the UK bankruptcy?

Answer:

1. The Insolvency (Cross-border) Act, 2006, which introduced the UNCITRAL Model Law into New Zealand law, provides a mechanism for Ms. Finder to approach the High Court to recognize the UK bankruptcy in New Zealand as a foreign proceeding and the UK as the center of main interests or COMI. The Model law makes it mandatory that the insolvent's "place of habitual residence", as required by section 16, schedule 1 of the Insolvency (Cross-border) Act, 2006, be the UK.
2. Heath J in Williams v Simpson (17 September 2010 High Court (Hamilton Registry)) noted that SCHEDULE 1 (i.e. the Model law) applies "when assistance is sought in New Zealand by a foreign representative (of an insolvent estate) in connection with a foreign proceedings" (at [38]. At [39], Heath J points to the difference between a "foreign main proceeding" and a "foreign non-main proceeding".
3. Given the definition of "center of main interest" in the Act, and how that is to be established, it cannot be said that Mr. Strong, although previously resident in the UK, has his place of habitual residence in the UK. Rather, it seems his current habitual place of residence is in New Zealand. Thus, Ms. Finder might not convince the court to declare that she, as foreign representative, and the UK bankruptcy be recognized as a foreign main proceeding.

4. Moreover, the New Zealand Bank intends pursuing Mr. Strong for the shortfall and therefore it is unlikely that a New Zealand court will grant an order which will adversely affect the rights of a New Zealand entity to pursue and attach Mr. Strong's assets in satisfaction of the shortfall.

Might want to consider reciprocal access to UK assets or stay enforcement by trustee, so NZ creditors get equal access to assets.

[Type your answer here]

*** End of Assessment ***