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THE LIQUIDATION PROVISIONS OF THE COMPANIES ACT 1993 - ARE CREDITORS BETTER OFF?

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ABSTRACT

This paper examines the liquidation provisions of the Companies Act 1993, in order to ascertain how effective those provisions are in protecting the rights of creditors of companies in liquidation. In particular, it focuses on the relationship between the liquidator and the creditors, and the impact of the reforms on that relationship.

The writer concludes that the reforms will bring New Zealand into a unique position among Commonwealth countries, all of which have recently reviewed their insolvency regimes, and all of whom have elected to retain the multiple process system. It is considered that the reforms are not consistently worked through in the new legislation. It is also argued that the removal of the ability of courts and creditors to sanction the actions of liquidators will result in a considerable reduction in the protection afforded to creditors. In addition, it is argued that the position of secured creditors has been significantly eroded. The writer's overall conclusion is that the reforms are prejudicial to the interests of creditors.

The text of this paper (excluding contents page, footnotes, bibliography and annexures) comprises approximately 15,000 words.

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I. INTRODUCTION

In the shadow of controversial reforms such as increased directors' duties and the ability of companies to purchase their own shares, changes enacted in the Companies Act 1993 to the liquidation regime applying to companies have escaped the glare of extensive publicity. This is perhaps because the new provisions are perceived to be an interim measure, pending a full-scale review of New Zealand's insolvency laws, which all governments in the past five years have promised as a priority for legislative reform.

However, despite the lack of attention, the changes to the liquidation provisions are far-reaching, and are likely to have a considerable impact on the commercial community. Most other Commonwealth jurisdictions have reviewed their insolvency laws during the last decade[1], including their laws relating to the liquidation of insolvent companies. All have considered that the traditional regime based on the English model developed late last century and early this century, works reasonably well in practice. Separate processes for voluntary, involuntary, solvent and insolvent liquidations have been retained in those jurisdictions, and the rights of creditors have been maintained, and in some instances, enhanced. It is the contention of the writer that the rights of creditors have been better protected by the retention of the traditional regime than creditors of New Zealand companies will be by the reforms introduced in the Companies Act 1993.

The New Zealand Law Commission, in its review of the liquidation regime[2], took as its touchstone the desirability of simplifying the current multi-tracked process. It therefore reduced the multi-tracked procedures to a single procedure, regardless of the solvency of the company or the voluntariness of the liquidation. In a further move to

[1] Australia introduced substantial reforms earlier this year; and the United kingdom introduced a new Insolvency Act in 1986.

[2] Reported in its *Report No. 9 - Company Law Reform and Restatement,* June 1989, Wellington.

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simplify and speed up the liquidation process it removed the need to obtain the sanction of the court or committee of inspection before undertaking certain steps in the liquidation.

This paper examines the impact of these reforms on the protection of creditors of companies in liquidation. In particular it focuses on the impact that the changes to the role of the liquidator have on the protection of creditors. The liquidator is the lynch-pin of the liquidation process; and the effects of the reforms on the liquidator's ability to administer a liquidation will have flow-on effects on the protection afforded to creditors. One of the stated aims in the long title to the Act is: "To provide straightforward and fair procedures for realising and distributing the assets of insolvent companies". This paper will consider whether that aim has been achieved from the point of view of creditors.

The paper proceeds on the assumption that the protection of creditors is an important aim of any companies legislation, including provisions relating to the demise of companies. As pointed out by the learned authors of the report of the United Kingdom Review Committee on Insolvency Law and Practice (known as the "Cork Report")[3]

> Credit is the lifeblood of the modern industrialised economy. The most significant extenders of credit are banks and other lending institutions such as finance houses or building societies. Manufacturers extend credit to customers and customers to manufacturers; the trade supplier extends credit to his customer; creditors are the cornerstone of the trading community. The employee who is paid at the end of the working week gives credit to his employer. Even the Government itself extends a form of credit by obliging employers and others involuntarily to act as tax collectors, for example, for PAYE and VAT.
>
> Credit is fundamental to trade, commerce and industry, whether the money is intended to be outstanding for a short term only or for a medium or long term and whether secured or unsecured. . .

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[3] *Insolvency Law and Practice* Report of the Review Committee, June 1982, London

In an address to the New Zealand Law Society conference earlier this year[4], it was contended that:

> It seems clear enough that, for capitalism to flourish, *creditors should be cherished.* All things being relative, such cherishing must take into account the ability of contemporary large creditors to seek their lending business in parts of the world that are more rather than less protective of their interests.

The writer respectfully concurs with the view that the protection of creditors should be one of the most important aims of any liquidation regime. It will be argued in the course of this paper that, as a result of the reform process itself, as well as of the substance of the reforms, the Companies Act 1993 does not altogether achieve such an aim.

II LIQUIDATION UNDER THE COMPANIES ACT 1955

A. Overview

The winding up provisions of the Companies Act 1955, of which there are some 131, together with the 193 rules contained in the Companies (Winding Up) Rules[5], form a winding up code. By that is meant that companies may not be wound up by any method other than that set out in the Act and its subordinate legislation[6]. The provisions, as with most of the Act, are based on the English model.

The method of appointment of liquidators under the Act, and the process by which the liquidation is conducted, vary depending on whether the winding up is court-ordered or voluntary, and on whether in the case of voluntary windings up, the company is solvent or

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[4] *Creditors and Certainty* A paper presented to the New Zealand Law Conference, Wellington, March 1993, Jack Hodder.

[5] The Rules contain substantive liquidation law, as well as High Court procedure and the day to day procedure of administering a liquidation.

[6] McPherson *The Law of Company Liquidation (3.d)* The Law Book Company Limited, 1987, at page 3

insolvent. There is no correlation between the solvency of a company and the voluntariness of the winding up. A solvent company can be forced into liquidation, and its insolvent counterpart can voluntarily choose to go into liquidation. In New Zealand, by far the majority of liquidations commence by order of the court. The next most common type of liquidation is the creditors' voluntary winding up, and there are a few members' voluntary windings up every year[7].

B. Court-ordered windings up

As far as the creditor/liquidator relationship is concerned, the significant features of the current regime in relation to court-ordered windings up can be summarised as:

a. Upon making a winding up order, the court must appoint the official assignee as provisional liquidator[8]. The provisional liquidator's primary task is to ensure that a permanent liquidator is appointed. The provisional liquidator must call separate meetings of both creditors and contributories of the company[9], in order to determine whether the application is to be made to the court for the appointment of a liquidator in the place of the official assignee.

   In practice, at present official assignees only rarely call such meetings. The official assignee is not obliged to call them if he or she considers that they need not be called (having regard to the assets of the company, the likely result of the winding up of the company, and any other relevant factor; and if, upon receiving notice from the official assignee of the intention not to call a meeting, the creditors or contributories do not require a meeting to be held[10]. If no meeting is held the official assignee becomes liquidator of the company.

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[7] See Appendix I

[8] s. 235(a) Companies Act 1955

[9] For definition of "contributory" see s. 212

[10] s. 235A Companies Act 1955

b. The liquidator is subject to extensive supervision by the court. First and foremost, the liquidator in a court-ordered winding up is an officer of the court[11]. There are certain powers which may be exercised by the liquidator only with the sanction of the court or the committee of inspection[12]. The liquidator requires sanction to:

i. bring or defend any action or other legal proceedings in the name of or on behalf of the company;

ii. carry on the business of the company;

iii. appoint a solicitor to assist in the conduct of the liquidator's duties;

iv. pay any classes of creditors in full;

v. make any compromise or arrangement with creditors;

vi. make any compromise or arrangement with contributories or debtors[13].

In addition, there are a number of powers and duties which are exercisable by the court, set out in sections 250 to 265 of the 1955 Act. Some of these may be delegated to the liquidator[14], and in such cases they are to be exercised by the liquidator as an officer of the court, and are subject to the control of the court[15].

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[11] See section 266 Companies Act, and *Re Timberland Ltd; Corporate Affairs Commission* v *Harvey* (1979) 4 A.C.L.R. 259

[12] s. 240 Companies Act 1955

[13] s. 240(1) Companies Act 1955

[14] s. 266 Companies Act 1955

[15] s. 266 Companies Act 1955

c. The liquidator is also subject to the scrutiny and control of the creditors. The liquidator is bound to "have regard to" directions given by resolution of the creditors or the committee of inspection[16]. In addition, the liquidator must summon general meetings of creditors if required to do so by resolution of the creditors, and can summon such meetings at any time he or she desires[17].

d. The liquidator can be released from the office only by order of the court, even if he or she has already resigned or been removed form office[18]. This is a logical result of the liquidator's status as the court's officer. Importantly, a release by the court from the office of liquidator also releases the liquidator from liability for the administration of the liquidation, although there are exceptions to this rule if the liquidator fails to disclose material information[19]. This provision clearly has a negative impact on the ability of creditors to pursue liquidators in respect of their conduct of the liquidation.

C. Voluntary windings up

In recent years, under half of all windings up annually have been voluntary windings up[20]. Both types of voluntary winding up (members' and creditors') commence by way of a resolution of members to wind the company up[21]. The ability of the company's directors to make a declaration that the company is able to pay its debts as they fall due for the period of 12 months from the date of the resolution (known as a declaration of solvency), determines which of the two types of winding up will take place[22].

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[16] s. 241 Companies Act 1955

[17] s. 241(2) Companies Act 1955

[18] s. 246 Companies Act 1955

[19] s. 246(5) Companies Act 1955

[20] See Appendix I

[21] s. 276 Companies Act 1955

[22] s. 274 Companies Act 1955

D. *Members' voluntary windings up*

If the company is solvent, the winding up proceeds under sections 275 to 282 of the 1955 Act. It is not proposed to discuss this mode of winding up in any detail, because by definition creditors will be paid out in full, and thus have little need for protection. In connection with the interests of creditors, the salient features of a members' voluntary winding up can be summarised as:

a. The liquidator is appointed and his or her remuneration is fixed by the company in general meeting[23]. The liquidator is not, therefore, an officer of the Court, although the creditors do have the right to apply to Court to have questions determined or to ask the Court to exercise any of the powers it is able to exercise in court-ordered windings up[24].

b. At the conclusion of the liquidation, there is no provision whereby the liquidator can be released from liability. The company's creditors therefore retain the right (subject to the normal effects of limitation periods under the Statute of Limitations) to pursue the liquidator in respect of his or her administration of the liquidation.

c. Creditors do not participate in the winding up process, and except in exceptional cases, a court will not be involved in the process either.

E. *Creditors' voluntary windings up*

This is the procedure used for a voluntary, insolvent winding up[25].

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[23] s. 276. Note that under s. 295 the court can appoint a liquidator if no liquidator is acting, and can remove a liquidator on being shown cause, and replace the removed liquidator; however, the company retains the power to appoint a replacement liquidator upon a vacancy, under s. 277

[24] s. 298 Companies Act 1955

[25] This type of winding up was introduced into English legislation after the report of the Greene Committee in 1926, which pointed out the "highly anomalous" position which had existed up until then, where, even if the company was insolvent, liquidation took place entirely under the control of members, rather than the

The provisions of the Companies Act 1955 pertaining to a creditors' voluntary winding up are:

a. A meeting of creditors must be summonsed by the company for the day of or the day after, the meeting at which the winding up resolution is made by the members. At the creditors' meeting the creditors can nominate a liquidator. If the creditors' nominee is different from the liquidator appointed by the members at their earlier meeting, the creditors' nominee shall prevail[26].

b. The creditors can appoint a committee of inspection of up to three persons. If they do so, the company can appoint up to three persons to also join the committee[27].

c. The committee of inspection, or if none, the creditors, are responsible for fixing the liquidator's remuneration.

d. Upon appointment of the liquidator all powers of the directors cease, except to the extent sanctioned by the committee of inspection or if none, by the creditors.

e. The liquidator has the same power as in a members' voluntary winding up to sell property of the company for consideration other than cash, but requires the sanction of the committee of inspection or the creditors to do so[28].

f. The winding up is concluded after the liquidator has submitted the final account of the winding up to a meeting of the company and a meeting of the creditors. A copy of the account and a return are filed with the Registrar of Companies, and at the

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creditors. It had been noted that the position was frequently abused by members, who appointed liquidators who would collude with those members to suppress evidence of fraud and mismanagement. The underlying theory of the new method suggested by the Greene committee was to give control over the insolvent winding up to those most directly affected by it - the creditors.

[26] Subject to court order on application of a director, member or creditor - s. 285 Companies Act 1955

[27] s. 286 Companies Act 1955

[28] s 288 Companies Act 1955

expiry of three months from the filing of that notice, the company is automatically dissolved[29]. There is no provision whereby the liquidator can apply for a release from liability.

III. THE CURRENT REGIME - PROTECTION OF CREDITORS

From the above description, it can be seen that protection of creditors under the Companies Act 1955 is tailored to each specific type of winding up. At one end of the scale is the members' voluntary winding up, for which very little creditor protection is provided, given that creditors in such winding up are at little risk. At the other end of the scale is the court-ordered winding up, which regime contains extensive creditor protection. The measures for protection of creditors in creditors' voluntary windings up lies between the other two types of winding up.

The most significant creditor protection measure in the 1955 Act court-ordered winding up regime is the extensive supervisory role of the Court. Section 240 ensures that actions of a liquidator which may put the creditors at risk are overseen by an independent party. It may be argued that a court is not the best-qualified forum for such oversight, and that some judges may lack the necessary skills to exercise meaningful supervision in the liquidation context, but the effect of the provision is to provide some sort of check and balance on the actions of the liquidator. As will be discussed below, the 1993 Act dispenses in all cases with the need of a liquidator to obtain sanction of the court prior to undertaking any act, unless he or she chooses to apply for directions.

As an extension of the court's supervisory role in court-ordered liquidations, is the liquidator's role in such liquidations as an officer of the court.

By virtue of section 240 the committee of inspection is also a powerful creditor protection mechanism. It can act as a substitute for the court,

[29] s. 291 Companies Act 1955

in granting sanction of the specified activities of the liquidator. As the committee is at least 50% comprised of creditors it is obviously a very effective means of ensuring that creditors' interests are monitored and protected. Under the 1993 Act, the name of the committee is, significantly, changed to "liquidation committee", reflecting its much reduced role and powers in the liquidation process.

A further protection of creditors is the obligation on liquidators to provide creditors with information, both as to the financial state of the company upon liquidation, and of the conduct of the liquidation. The liquidator is obliged to call meetings of creditors, and to supply creditors with a report as to the affairs of the company. As will be discussed below, in light of the reduction of other forms of creditor protection, the 1993 Act purports to place greater obligations on the liquidator to provide such information to creditors, with the introduction of such requirements as the six-month report to creditors. However, as will be discussed later in this paper, the exceptions to these rules are so extensive as to seriously undermine their usefulness as a protection to creditors.

The 1955 Act also allows a more direct role in the liquidation to be taken by creditors by way of the meeting of creditors. The meeting has the power to elect a liquidator to replace the person appointed by the court (in the case of court-ordered windings up), or by the members (in the case of creditors' voluntary windings up). This ability to have a say in who acts as liquidator was initially absent from the Bill, as will be discussed below, but was reinserted into the new Act. The liquidator must have regard to the views of the creditors, as expressed by them in meetings. It may be thought that with the removal of the supervisory role of the Court, and the reduction in the power of the committee of inspection, the role of the creditors may have been increased under the new legislation accordingly. However, as will be discussed below, that is not the case.

Finally, any control on who may act as a liquidator is designed to be a protection for creditors. The 1955 Act, in fact contains very few restrictions on who may be a liquidator, and although the Law Commission in its report advocated that only "qualified persons" as

defined by the Commission, should be permitted to act as liquidator, this protection was not carried through into the Act, as will be discussed below.

IV PROCESS OF LIQUIDATION

A. Reduction to a Single Process

The single most important change in the liquidation provisions of the Bill is the reduction down to one process of the several different types of processes which currently exist under the 1955 Act. Apart from some procedural differences immediately upon the commencement of liquidation, creditors now face essentially the same procedures whether a company is solvent or insolvent, and whether its liquidation is forced upon it by court order or entered into willingly. This reform renders the New Zealand regime unique among Commonwealth jurisdictions; but strangely, given the potential impact of the reform on the interests of creditors, it has not received a great deal of attention by way of submissions to the select committee or in the media[30], and the merits of the single system of liquidation do not appear to have been widely canvassed.

The Law Commission, in instigating the reform, based the proposal on its policy of simplifying company law. In its Report No 9 the Commission stated:

> At present there are five ways in which a company may be ended. The methods have different modes of commencement, different procedures and different consequences. We do not see any purpose or justification for this complexity. We believe that the disbanding of companies should be possible with minimum formality . . . Liquidation can be applied to companies whether solvent or insolvent, and

[30] With the exception of the Society of Accountants, which made a number of submissions on the issues raised by the reforms at several stages of the reform process.

whether commenced by voluntary actions of the company or imposed by others[31].

C. The Bill

The first draft of the Bill, based on the draft proposed by the Law Commission in its Report[32], carried through in a pure form a single system of liquidation. As with the Law Commission draft Bill, once liquidation had commenced, absolutely no recognition was given to the differing circumstances which might have brought about the liquidation of the company. The draft sought to simplify procedures , and thus many procedural safeguards for creditors which are built into the 1955 Act had been discarded. These safeguards were replaced, the Law Commission draft, with the single, fundamental protection of allowing only experienced insolvency practitioners to act as liquidators[33]. With the guarantee of an expert and objective liquidator, the Law Commission believed that there was no longer a need for complex, expensive and lengthy procedural safeguards, such as the need to obtain sanction of the court to undertake various activities (in the case of court-ordered windings up), and the need to permit creditors to appoint their nominated liquidator (in the case of creditors' voluntary windings up).

The Bill did not, however, carry through the concept of the experienced insolvency practitioner, perhaps because of the prevailing governmental policy against occupational licensing, and the protection which it provided. Reaction to the pure single process introduced in the first draft of the Bill was sharp[34]. As a result, certain measures, giving creditors greater involvement in the liquidation process, depending on the state of solvency of the company were reintroduced[35].

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[31] Above, n.2 para 640

[32] Above, n.2

[33] Above, n.2 para 642

[34] In submissions to the Select Committee

D. Comparison With Other Jurisdictions

As stated above, the single system which the Bill contains is unique in Commonwealth and, as far as the writer can ascertain, in United States jurisdictions.

1. United Kingdom

A distinction is drawn between solvent and insolvent companies in the United Kingdom. Insolvent companies are wound up under the Insolvency Act 1986. Although legislating for both personal and company insolvencies, the UK Insolvency Act (unlike the Canadian and United States Bankruptcy Act) does not assimilate the law relating to individuals and companies into one regime. Rather, the Act sets out two quite separate regimes - Part I of the Act dealing with companies, and Part II dealing with individuals. The Act was introduced in 1986 after an intensive law reform exercise based around the Cork Report[36].

As with the New Zealand 1955 Act, the Act provides that winding up can commence either by order of the court, or voluntarily[37]. In addition, it retains a distinction in the case of voluntary winding up between creditors' and members' windings up[38], with the factor determining which type will take place being the ability of the directors to make a declaration of solvency. The Act deals with solvent windings up, in the same way as under the New Zealand Act, despite the title of the Act [39]. In a court-ordered winding up the official trustee is appointed by the court in every case[40], and the creditors and contributories later have the right at their respective meetings to resolve to appoint another liquidator. The court appoints a liquidator

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[35] cl. 220A - cl 220C of the Bill, which will be discussed in more depth below

[36] Above, n.3

[37] s.73 Insolvency Act 1986 (UK)

[38] s.90 Insolvency Act 1986 (UK)

[39] The long title to the Act states that the Act is "to consolidate the enactments relating to company insolvency and winding up (including the winding up of companies that are not insolvent, and of unregistered companies). . ."

[40] s.136 Insolvency Act 1986 (UK)

only in the case of a dispute between the contributories and the creditors over who should be appointed as liquidator. In all material respects the regime is the same as that presently in force in New Zealand. The only minor differences are:

a. There is provision for the release of liquidators in the case of voluntary windings up[41];

b. In the case of creditors' voluntary windings up, until such time as the creditors can meet to determine whether to appoint their own liquidator, the liquidator appointed by the company must apply to court before carrying any actions in relation to the liquidation apart from the following duties:

(i) to take into custody or control property to which the company is or appears to be entitled;

(ii) to dispose of perishable goods and other goods if their value is likely to diminish if not immediately dealt with; and

(iii) to do all things appropriate to protect the company's assets.[42]

c. If a company has a paid up capital of not more than 120,000 pounds, the county court has concurrent jurisdiction with the High Court to wind up the company.

2. *Canada*

In some jurisdictions in Canada, companies which are solvent, or have obtained the consent of their creditors can terminate their existence by surrendering their charter or certificate of incorporation .

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[41] s. 173 Insolvency Act 1986 (UK)

[42] s. 166 Insolvency Act 1986 (UK)

Under federal or provincial legislation, a company may be wound up under various grounds, but not on the grounds of insolvency. Insolvent companies must be wound up under either the provisions of the Bankruptcy and Insolvency Act, or the Winding Up Act, both of which are federal Acts.

Under the Bankruptcy and Insolvency Act (the title of which was amended in 1992 by the addition of the word "insolvency" as a consequence of certain amendments which apply to debtors who are insolvent, but not necessarily bankrupt), the court can make a "receiving order" [43], appointing a trustee, in whom all property of the company vests. The company continues in existence, and the powers of the directors and officers of the company are not affected by the bankruptcy, although in practical terms will obviously be restricted by virtue of the fact that the company's property is vested in the trustee. The trustee must summon a meeting of creditors, and the meeting may appoint a number of inspectors (up to five)[44]. The trustee must have regard to the directions of the creditors and the inspectors in the administration of the estate. The trustee's duties are to get in all of the assets of the company, collect claims against debtors, enforce the liability of unpaid shares[45], and distribute dividends to creditors.

Only if it has satisfied the claims of its creditors in full can a company be discharged from bankruptcy[46]. In such a situation, the company will normally have obtained a discharge and then proceed to wind up voluntarily.

Alternatively, companies can be wound up under the Winding Up Act. This legislation provides for the liquidation of the company, as opposed to its bankruptcy. The Act applies to solvent and insolvent companies. In the case of insolvent winding up, the court makes an order upon petition. Upon winding up, a provisional liquidator is

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[43] s. 43 Bankruptcy Act (Canada)

[44] s. 116 Bankruptcy Act (Canada)

[45] s.16 - s.28 Bankruptcy Act (Canada)

[46] s. 169(4) Bankruptcy Act (Canada)

appointed, and the matter is referred to an officer of the court to appoint a permanent liquidator, although the court can appoint a liquidator at the hearing of the petition. In all other material respects the provisions are very similar to the 1955 Act, although the court retains closer control over the conduct of the liquidation. For example, the liquidator must bring to court a list of disputed claims, and will serve notice on creditors to appear and prove the claim before the court.

3. Australia

The Australian Corporations Law provides for two modes of winding up - court ordered or voluntary. Major reforms to the provisions relating to winding up by the court, introduced by way of the Corporate Law Reform Act 1992 came into force on 23 June, 1993. These were brought about as a result of the recommendations of the Australian Law Reform Commission's report entitled "General Insolvency Enquiry" - known as the Harmer Report. The provisions relating to court-ordered winding up are now divided into two parts - one dealing with what is now termed "winding up in insolvency"[47], and the other termed "winding up by the court on other grounds"[48]. In addition, the distinction in voluntary windings up between members' voluntary windings up and creditors' voluntary windings up is maintained.

Overall the provisions, although more detailed and extensive than the New Zealand Act (consisting of approximately 250 provisions), are in most respects similar to those set out in the New Zealand Act. The major differences can be summarised as:

a. The new division relating to insolvent court-ordered windings up includes an extensive definition of insolvency[49], and introduces rebuttable presumptions of insolvency to replace the previous deeming provisions[50]. Once the company is wound up, though,

[47] Part 5.4

[48] Part 5.4A

[49] s. 95A

it is subject to the same creditor and court involvement whether it is solvent or insolvent.

b. Overall court and creditor involvement in the conduct of the liquidation is lower than that under the current New Zealand legislation. A liquidator requires sanction only for:

- a compromise of a debt in excess of $20,000; and
- the execution by a liquidator of a long-term agreement on behalf of the company[51] (long-term being in excess of three months).

c. In the case of voluntary windings up, the liquidator requires sanction before exercising the same powers as those requiring sanction in a court-ordered winding up. In the case of a creditors' voluntary winding up the sanction may be from the court, committee of inspection, or resolution of creditors; in the case of a members' voluntary winding up, it must be from a resolution of members.

d. Methods of appointing liquidators vary from State to State, but the question of who may act as a liquidator is very tightly regulated. All liquidators must be registered by the local State office conducting the regulation of companies. Criteria include appropriate educational qualifications, evidence of good fame and character, extensive experience in insolvency practice, and non-disqualification from being registered. In addition, a person may be appointed or registered as an official liquidator (and thus eligible to be appointed as a liquidator in a court-ordered liquidation). Such appointment is an entirely discretionary process.

e. In a creditors' voluntary winding up, a liquidator appointed by the members must obtain approval of the court in order to take

[50] s. 459C - c.f. s. 218 of the NZ Companies Act 1955

[51] s. 477

certain acts prior to the creditors having an opportunity to appoint their own liquidator.

4. United States

Companies can be wound up either via the federal bankruptcy laws[52]. or by way of non-bankruptcy liquidation. In addition, there is the ability to reorganise, which is beyond the scope of this paper, and will not be further discussed.

Non-bankruptcy liquidations (solvent liquidations) under all statutes involve, as with the Westminster model, the collecting in of the assets of the company, the payment of expenses and debts, and distribution of the net assets to the shareholders of the company, according to the priorities set out in the particular state statute[53].

Liquidation under such statutes can be commenced either by the court, or by the company. Where the liquidation is "non-judicial", the court's supervision can be invoked.

Insolvent corporations are liquidated under the federal bankruptcy laws[54]. Although some states have statutes dealing with the liquidation of insolvent corporations[55], when the provisions of such statutes conflict with the federal statute, the federal legislation prevails. Bankruptcy of a company along the lines of a liquidation under the New Zealand companies legislation is dealt with in Chapter 7 of the Code, and is known as 'straight bankruptcy'. Bankruptcy can be involuntary at the suit of creditors, or other parties, or voluntary, at the suit of the company itself. A "trustee" is appointed - either a state-appointed trustee, known as the US trustee, or another trustee

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[52] Bankruptcy Code Title 11 United States Code

[53] See Henn & Alexander *Laws of Corporations (3.d)* 1983 St Paul, Minn. West Publishing Co., where various examples of such statutes are cited.

[54] Above, n. 52

[55] For example, N.Y. Bus. Corp. Law, para 1202 ff.

appointed by a meeting of creditors[56]. The trustee's duty is to "collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of the parties in interest"[57]. A creditor's committee of between three and eleven members can consult with the trustee, make recommendations regarding the trustee's conduct of the bankruptcy, and submit any questions regarding the bankruptcy to the court or to the US trustee[58]. Corporations cannot be discharged from bankruptcy[59].

5. Discussion

(a) General

It can be seen, then, that the single liquidation process introduced by the 1993 Act is unique. All of the other jurisdictions considered differentiate at least between solvent and insolvent liquidations. As proposed in the Harmer report, the Australian Corporation Law has gone so far as to make this explicit in its terminology, by introducing a new Division entitled "Winding Up in Insolvency" . The authors of the report state[60]

> The existing terminology of "winding up" applies to the process of administering the affairs of both solvent and insolvent companies. It can be confusing and misleading, It creates a perception that any company which is being wound up is insolvent. This may cause misunderstanding and prove embarrassing to those who are associated with solvent companies undergoing a winding up process.

(b) Solvent windings up

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[56] Paragraphs 701-703 Bankruptcy Code

[57] Paragraph 704 Bankruptcy Code

[58] Paragraph 705 Bankruptcy Code

[59] Paragraph 727 Bankruptcy Code

[60] The Harmer Report, para 21

In the case of a solvent winding up, all creditors, by definition, will be paid in full. They therefore have no financial interest in the winding up of the company [61]. It could be argued that indeed any involvement by the creditors in the process will have an adverse effect on the speed and expense involved in winding the company up. The provisions of the 1993 Act however, permit quite extensive creditor involvement in solvent windings up. Although under section 243(8) a liquidator of a solvent company which has been put into liquidation by the company or the board (i.e. essentially voluntarily) is not bound to call a meeting of creditors to consider the appointment of their own liquidator, a liquidator may cause such a meeting to be called in the case of a court-ordered solvent winding up[62]. In addition there is no restriction in the case of solvent liquidations on the rights of creditors to call meetings of creditors[63], or to appoint liquidation committees. In addition, the liquidator is subject to the duties of settling a list of creditors; preparing and forwarding to creditors a statement of affairs and initial report; and preparing and forwarding six-monthly reports to creditors[64]. All of these duties are time-consuming and may involve considerable expense. Ironically, the less solvent a company is, the less likely a liquidator is to be subject to these duties. If the liquidator is satisfied that the value of the assets available for distribution to creditors is not likely to exceed 20 cents in every dollar, the liquidator is not required to carry out the duties laid down in section 255(5)[65]. This exemption will not, of course, apply to a solvent company, and if a liquidator wishes to avoid the duties an application to the

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[61] See above, n.6 at page 28

[62] As is the case under the current Act

[63] Under s. 258 Companies Act 1993

[64] s. 255 Companies Act 1993

[65] Under s. 255(4)

court under section 255(4) is necessary. It appears, therefore, that the liquidator is bound to incur time and expense either in carrying out the duties or in making an application to avoid doing so. It seems difficult to justify the cost of what are creditor protection measures in circumstances where creditors do not, by definition, require such protection.

(c) *Insolvent windings up*

The tenor of the submissions of both the Society of Accountants[66] and KPMG Peat Marwick[67] to the Minister of Justice clearly indicated that, in the view of those organisations, what are presently known as creditors' voluntary windings up work well in practice. In its 1987 discussion paper the Australian Law Reform Commission[68], suggested that the distinction between a court-ordered or compulsory winding up and a creditors' voluntary winding up be extinguished. However, by the time the Commission produced the Harmer Report in 1988, it was clear that it had discarded this notion. It identified only two aspects of the creditors' winding up process which it considered unsatisfactory: the absence of some ordered administration between the time of calling the meetings of creditors and contributories and the appointment of a liquidator ; and the lack of independent information about the financial affairs and conduct of the business of the company at the meeting of creditors. The authors of the Cork report[69]

The voluntary procedures for winding up insolvent companies appear to have worked reasonably well for many years and,

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[66] By submission dated 1 March, 1993

[67] Dated 25 February, 1993

[68] DP 32, page 11

[69] Above, n.3 at page 154

save in one respect we do not believe that any major changes are necessary in their practical application.

Although the Cork report advocated the abolition of the title "creditors' voluntary winding up", on the grounds that "though explicable on historical grounds, is somewhat misleading; it has been represented to us that confusion sometimes arises over the precise difference between a members' and a creditors voluntary winding up", the terms were carried forward into the United Kingdom Insolvency Act 1986.

It can be seen therefore, that despite debate and initiatives to abolish the creditors' voluntary winding up process, it has survived intact, indeed in enhanced form, in other jurisdictions. The creditors' voluntary winding up is an attractive alternative to a court-ordered winding up because of its relatively streamlined administration compared to a court-ordered insolvent winding up. The creditors avoid the time and expense of applying to court for a winding up order, but derive protection from their involvement in the liquidation process and their ability to apply to the court if the need arises. The liquidator has greater autonomy than a liquidator in a court-ordered winding up, and can thus get on with the duties of getting in the assets of the company and realising them. The problem identified in the Harmer and Cork reports of the need to restrict the activities of the company or liquidator appointed by the members prior to the creditors' meeting does not seem to have arisen in New Zealand or to have been discussed by New Zealand commentators. It is the writer's view that most of the advantages of the creditors' voluntary winding up have been preserved in the 1993 Act. There are a few caveats to that assessment however.

The provisions of the Bill, as first drafted, had a negative impact on the protection of creditors in an insolvent,

voluntary winding up. There was no ability for creditors to appoint their own liquidator or for a meeting of creditors to be called early on in the liquidation. This defect was partially rectified by the insertion of clauses 220A to 220C of the version of the Bill reported back from the Select Committee (now sections 243-245 of the 1993 Act). Under the reported-back version of the Bill there were, however, several difficulties with the operation of these provisions, one of which was the inordinately long time-limits which the clauses set down for the calling of a meeting of creditors, or of advising creditors that the liquidator proposes to call no such meeting. Under current law[70], unless the company's directors make a declaration of solvency within 30 days before the winding up resolution, the company must call a meeting of creditors for the same day as, or the day after the day the winding up resolution is passed. Under the 1993 Act, a liquidator must call a meeting of creditors to determine whether to pass a resolution specifying a time or times that creditors' meetings should be called[71] . As originally drafted under the reported-back version of the Bill, notice of the calling of the meeting of creditors had to be given in all cases within 40 days of the commencement of the liquidation, at the latest, since the notice had to accompany the liquidator's initial report required under section 255 (2) There was a gap in the Bill, in that it does not provide for when such notice shall be given in the case where a liquidator is exempted from the requirement to provide an initial report under section 255. These problems have been rectified under the 1993 Act. However, as will be discussed below, even as amended, these time limits may well have an adverse effect on the protection of creditors due to the actions of the liquidator first appointed by the members. In

[70] s. 284 Companies Act 1955

[71] s. 258(1)(b) Companies Act 1993

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addition, the whole liquidation process is slowed unnecessarily.

In addition the new Act reduces creditor protection through the removal of the need for creditor sanction for certain actions. In this respect the Act goes further even than the Australian legislation by removing completely the need to obtain sanction for any act. This departure will certainly have an adverse effect on the protection of creditors, at least in those liquidations where a dividend of less than 20 cents in the dollar is expected. The removal of the need of the liquidator to obtain sanction may be balanced by the provisions of the Act[72] increasing the amount of information a liquidator is bound to provide to creditors. Armed with such information the creditors can arrange for a meeting of creditors to be called, through which to express their views[73], or alternatively, can apply to court to have the liquidator's decision or action considered there[74]. However, a liquidator is not subject to the information duties where it is anticipated that the dividend to the unsecured creditors will not exceed 20 cents in the dollar[75]. This exception seriously erodes the justification for removing the requirement to obtain sanction. In such very insolvent liquidations it will be a considerable advantage to creditors to appoint a committee of inspection to supervise the liquidator, and to act as a conduit of information to the other creditors.

(*d*) *Court-ordered windings up*

In the case of involuntary, insolvent liquidations (by far the majority of liquidations in New Zealand)[76], again the

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[72] s. 255

[73] s. 258

[74] s. 286

[75] cl. 255(4)

Act's reforms go a great deal further than those in other jurisdictions, as far as a reduction of court and creditor supervision of the liquidator is concerned. This aspect of the reforms will be discussed in more detail below, in the context of a practical example. In addition, the same initial difficulties arise as in a voluntary insolvent liquidation, as to the extent to which a liquidator first appointed by the court may act. However, it is this type of liquidation which is least affected by the provisions of the Act, and many of the provisions of the liquidation section seem to fit most comfortably into the insolvent, non-voluntary context. Of all types of liquidation, creditors' interests appear to suffer least from the reforms in this type of liquidation.

V. THE LIQUIDATOR

As discussed in the introduction to this paper, the liquidator is the lynch-pin of the liquidation process[77].

A. The Liquidator's Principal Duty

Section 253 of the Act sets out the liquidator's principal duty. Essentially, this provision is the cornerstone of Part XVI. The other

[76] See Appendix I

[77] The title "liquidator" dates from the Joint Stock Companies Act of 1856, although under that legislation the position of liquidator was more analogous to an assignee in bankruptcy than to a modern liquidator. The corporate personality of the company ceased upon the appointment of the liquidator, when all property of the company became vested in the liquidator. Under modern company winding up law, the notion of corporate personality is carried through into the winding up period, and upon appointment, the liquidator assumes the office and powers of the directors of the company. The liquidator's position consists of a range of functions and relationships. First and foremost, the liquidator is a creature of statute, and is subject to the provisions of the relevant Act. In some cases (in court-ordered liquidations, and always, in the case of official liquidators) he or she is an officer of the court. In relation to the company's creditors, it has been stated that: "it is impossible to be definite about the precise nature of the legal relationship which exists between a liquidator and the creditors . . . of a company in liquidation" , but the position has been described as being similar to that of a trustee or quasi-trustee, but without all of the powers and duties of a trustee. The liquidator certainly owes a fiduciary duty to the company, and almost certainly to the creditors and shareholders of the company. The liquidator's powers and duties range from purely administrative through to quasi-judicial, often calling for acute commercial judgement in difficult circumstances. To add to the challenge of the position, although the liquidator takes on the powers and office of directors, liability for his or her actions is not limited, and in various circumstances the liquidator is exposed to personal liability; and all this in a situation where he or she is under a duty not to profit.

powers and duties conferred upon the liquidator in Part XVI are, on the whole, designed to give effect to this provision. The clause is modelled on cl. 207 of the Law Commission's draft Bill[78]. In its commentary, the Law Commission stated that : " This statement of the common law is intended for clarity and completeness" [79].

The section provides:

> Subject to section 254 of this Act, the principal duty of a liquidator of a company is-
>
> (a) To take possession of, protect, realise, and distribute the assets, or the proceeds of the realisation of the assets, of the company to its creditors in accordance with this Act; and
>
> (b) If there are surplus assets remaining, to distribute them, or the proceeds of the realisation of the surplus assets, in accordance with section 313(4) of this Act-
>
> in a reasonable and efficient manner.

Given the importance of section 253 in the scheme of the liquidation regime, it is suggested that its drafting is somewhat imprecise. For example, the provision has been amended since the first draft of the Bill in an apparent attempt to clarify the fact that a liquidator can make distributions either in specie or of the proceeds of realisation of the sale of the assets. The words "or of the proceeds of the realisation of the assets" have been inserted, and presumably relate to the duty to distribute. However, the duty to realise has been left untouched, and there is thus an apparent contradiction between the duty to realise and the ability to distribute assets without realisation. In addition, it is unclear whether the phrase "in accordance with this Act" relates to the distribution to creditors, or to all duties set out in this section. While these are apparently insignificant technical defects, it is submitted that they could produce some uncertainty, which would clearly be adverse to the interests of creditors.

B Property Subject to a Charge

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[78] Above, n.2 at page 300

[79] Above, n.2, at paragraph 667

The duties outlined in section 253 are expressed to be subject to section 254. This provides that:

> Notwithstanding any other provisions of this Part of this Act-
>
> (a) Except where the charge is surrendered or taken to be redeemed under section 305 of this Act, a liquidator may, but is not required to, carry out any duty or exercise any power in relation to property that is subject to a charge:
>
> (b) Where-
>
> (i) A company is put into liquidation under section 241(2)(c) of this Act; and
>
> (ii) The Official Assignee is the liquidator of the company; and
>
> (iii) The company has no assets available for distribution to creditors of the company, -
>
> the Official Assignee shall not be required, without the consent of the Minister of Justice , to carry out any duty or exercise any power in connection with the liquidation if, to do so, would or would be likely to involve incurring any expense.

The exempting of the liquidator from exercising the duties in section 253 in relation to property subject to a charge, unless it is surrendered, is a reversal of the current position. The issue of whether a liquidator is bound to exercise any duties in relation to property subject to a charge was raised in *Re Your Size Fashions Limited*[80]. In that case, the official assignee became the official liquidator of Your Size Fashions Limited (in liquidation). The secured creditor (Westpac) refused to realise the assets secured by its debenture on the grounds that the cost of so doing would have exceeded the amount recoverable. Instead it demanded that the Official Assignee realise the charged assets on its behalf. It was economic for the Official Assignee to undertake the realisation because of the low rate of remuneration which the Official Assignee is permitted to charge under the relevant provision of the Companies Act 1955. Pending resolution

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[80] (1990) 5 NZCLC 66,804

of the matter by the Court, the Official Assignee refused to realise the secured assets, on the ground that there was no realistic possibility of any funds being available for unsecured creditors. He indicated to the secured creditor that only if appointed as the secured creditor's agent (with remuneration at the full market rates of a receiver), and if given an indemnity as to costs, would the he take any steps on the secured creditor's behalf. This was the normal procedural practice, where the unsecured creditors would not gain anything from the realisation.

Williamson J held that the liquidator could not so refuse. He held that a liquidator's duties extend to all creditors, and not just to those proving in a liquidation, and relied in support of this proposition on *Gooch's Case; re Contract Corporation*[81]. He also relied upon the wording of R58 of the Companies (Winding Up) Rules[82]. Finally, he relied on the proposition that property subject to a charge remains the property of the company, and the fact that "a secured creditor is entitled to stand aloof from the liquidation"[83].

In the first draft of the Bill, it appeared that the rationale of the predecessor to section 254(1) was to redress the situation which arose specifically in the case of an official liquidator, whose fees are statutorily set at a considerably lower rate than private insolvency practitioners would charge for the same service: in other words, where the secured creditor insists on a State-subsidised service. However, the subclause as originally drafted went much further than simply redressing this problem. It appeared to go so far as tying the liquidator's hands by preventing him or her from acting in relation to

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[81] (1872) 7 Ch App 207

[82] This Rule provides:
(1) The duties imposed on the Court by subsection (1) of section 251 of the Act in a winding up by the Court with regard to the collection of the assets of the company and the application of the assets in discharge of the company's liabilities shall be discharged by the liquidator as an officer of the Court subject to the control of the Court.
(2) For the purpose of the discharge by the liquidator of the duties imposed by subsection (1) of section 251 of the Act, and subclause (1) of this rule, the liquidator in a winding up by the Court shall, for the purpose of acquiring or retaining possession of the property of the company, be in the same position as if he were a receiver of the property appointed by the Court, and the Court may, on his application, enforce the acquisition or retention accordingly.

[83] Note that section of the Act circumscribes this ability of the creditor to stand aloof from the liquidation, as will be discussed below in the context of a practical example.

property subject to a charge. There are occasions where the creditors as a whole would benefit from the liquidator having such ability, for example where the company has a substantial equity of redemption in the asset, or in the case of property subject to a floating charge, which ranks behind preferential claims, and which a liquidator may wish to realise to satisfy the preferential claims[84].

In the Act, these criticisms have been addressed, by the provision in section 254(a) that the liquidator "may but is not required to " carry out the duties. In addition, a new provision, section 254(b), has been inserted into the Act. This addresses the position of the Official Assignee specifically. It provides that, where the company has no assets available for distribution to creditors, the Official Assignee is not required, without the consent of the Minister of Justice, to take any step in the liquidation, if to do so would be likely to incur an expense. This provision is essentially a re-enactment of Rule 175 of the Companies (Winding Up) Rules.

The new provision raises the issue of what is meant by a "creditor". Presumably the intention is that the section applies to non-secured creditors only (including preferential and unsecured creditors); on the basis that assets which are charged are not assets of the company "available for distribution". However, this contention was expressly rejected by Williamson J in the Case of *Your Size Fashions*[85]. The Official Assignee argued in that case that the assets of the company covered by Westpac's debenture were not "available assets". Westpac argued, on the other hand, that the debenture did not pass legal title, or possession, of the charged assets, and that they therefore were available assets. Williamson J., agreeing with Westpac, adopted the reasoning of Denning MR in the case of *Re Barleycorn Enterprises Limited*[86], and held that the same reasoning applies to the Companies Act 1955.

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[84] Such criticisms of the clause were raised in submissions to the Minister of Justice by the New Zealand Society of Accountants (1 March, 1993), and by Chapman Tripp Sheffield Young (25 May 1993)

[85] Above, note 80

[86] [1970] Ch. 465 (CA)

C Duty of Liquidator to Prepare Statement of Affairs

Under the Companies Act 1955, the directors of a company wound up by order of the Court are obliged to prepare a statement of the affairs of the company [87]. The statement must be verified by at least one director, and the secretary, or persons selected by the official assignee. Failure to furnish the statement is punishable by a fine for each day of default ($20), and in addition, the Court retains the jurisdiction to require the statement to be submitted[88]. There is no provision under current law which requires a statement of affairs to be prepared in the case of voluntary windings up.

The Law Commission, in its draft Bill, shifted the responsibility for the preparation of statements of affairs on to the liquidator[89]. The Commission indicated that it envisaged use of a simpler form than that currently prescribed[90]. It stated that the policy for the shift in responsibility was that:

> It is preferable that the liquidator compile reliable, if sometimes incomplete, information, and give that to the creditors and shareholders rather than expend resources on obtaining a statement of affairs from difficult directors[91].

This proposal has been carried through to the Act in section 255(2)(c)(ii)(A).

In the writer's view, it is questionable whether the Law Commission's rationale holds true in all cases. In the case of insolvent voluntary windings up, the requirement for a statement of affairs will no doubt enhance the protection of the company's creditors by adding to the

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[87] See s. 231 Companies Act 1955, and Rules 33 - 38 of the Companies (Winding Up) Rules

[88] See *Re New Par Consuls* [1898] 1 QB 573

[89] Above, n.2 cl.208 of the draft Bill

[90] Form 21 Companies (Winding Up) Rules

[91] Above, n.2 para 669

information available to them. In addition it gives the creditors the opportunity to inform the liquidator if they detect from the statement that she is proceeding on information which they know to be incomplete or inaccurate.

On the other hand, in the case of solvent windings up, it is questionable whether a statement of affairs is necessary at all. It is submitted that, given that the creditors will be paid in full, the affairs of the company are really of no interest to them.

The problem of reluctant directors is one which it is suggested is unlikely to be encountered in a voluntary winding up situation, as opposed to a court-ordered winding up where the liquidation order was made against the will of the directors. It is likely that the liquidator, being less familiar with the affairs of the company than the directors, will incur a greater cost both in time and in money in preparing the statement of affairs. It seems difficult to justify this in the case of liquidations which commenced voluntarily[92], where the policy reasons for shifting the responsibility do not appear to apply.

Even in the case of court-ordered liquidations (specifically insolvent, involuntary liquidations which is the type of situation which most readily lends itself to the Law Commission's analysis, in the writer's view, the policy for the change is questionable. In compiling the statement of affairs the liquidator is likely to require the assistance of one or more of the directors of the company to provide her with the requisite information. If a director is reluctant to prepare the statement it is most likely that he or she will be equally reluctant to assist the liquidator in preparing the statement of affairs. The creditors do not have the comfort of an effective sanction against directors for non-co-operation under the 1993 Act. Although bound to assist the liquidator, there does not appear to be a sanction for directors and other company officers who fail to do so[93]. The Law Commission may have recognised this in its reference to "incomplete information". Again, it is

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[92] i.e. where a liquidator is appointed by special resolution of the shareholders under section 241(2)(a), or by the board under section 241(2)(b)

[93] s. 261 Companies Act 1993

likely that, due to lack of familiarity with the affairs of the company, the liquidator will often incur a greater cost in preparing the statement of affairs than a director would do, and this of course reduces the funds in the estate available to creditors.

Although the issue of who prepares the statement does not at first glance appear to affect the question of where the cost of its preparation will lie, since in either case the liquidation will bear those costs, this may not always necessarily be so. In the unreported decision of *Re Hayes Garage Limited (In Liq.)*[94], the Court allowed a liquidator to deduct from the costs presented to him by a director for the preparation of the statement, the cost of work which should have been undertaken by the company before it was placed into liquidation. Such a sanction will not be available under the new provision, and if, as is often the case, the papers of the company are not up to date, the liquidation initially will have to bear the cost of the liquidator doing this or causing it to be done. This cost, will of course ultimately be borne by creditors. Creditors may gain some redress against the directors for failure to keep adequate accounts, if such failure has contributed to the company's insolvency[95], or via other directors' duties.

Another relevant factor, although of less importance, is the ability to detect errors or omissions in the statement of affairs. As well as providing information to creditors, the statement of affairs provides a basis for the liquidator's conduct of the liquidation. It is unlikely that a liquidator who has prepared a statement will be alert to information which would suggest that the contents of the statement are inaccurate or incomplete. The liquidator is more likely to approach a statement prepared by a director with a more discerning eye.

As far as comfort available to creditors in terms of sanctions is concerned, the position is effectively the same in the case of a liquidator preparing the statement as where a director prepares it. Under current law, defaulting directors are subject to an ongoing fine,

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[94] unrep. Christchurch, M9/76, Casey J

[95] under section 300 of the Act

In addition, if they produce a statement which is false or misleading they are liable upon conviction to a fine of up to $1000, or a prison sentence of up to two years[96]. The creditors therefore have the comfort of both the coercive and the deterrent provisions. The sanctions available against a liquidator recognise the fact that liquidators do not have the same motivation to mislead creditors that directors facing personal liability would have. If a liquidator failed to prepare the statement of affairs, a creditor would, however, have the ability to apply to the court under section 286 for failure to comply.

VI IMPLICATIONS OF CHANGE UPON DUTIES AND POWERS OF LIQUIDATORS ON PROTECTION OF CREDITORS

A. Interim Liquidators

Essentially, the 1993 Act carries through the current law relating to the appointment of provisional liquidators prior to the making of a winding up order[97]. While the 1955 Act does not expressly restrict the provisional liquidator to lesser powers than those conferred on a liquidator proper, it does confer the power on the court to limit and restrict the provisional liquidator's powers. It is now clear that a provisional liquidator's primary duty is "to preserve the status quo with the least possible harm to all concerned so as to enable the Court to decide after a proper and final hearing whether or not the company should be wound up"[98]. The new Act embodies this common law position in the language of section 246. An interim liquidator has rights and powers "to the extent necessary or desirable to maintain the value of assets owned or managed by the company"[99]. In addition, the court may limit the interim liquidator's powers further[100].

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[96] Ss 461 and 461E Companies Act 1955

[97] s. 234 Companies Act 1955

[98] *Re Chateau Hotels Limited* [1977] 1 NZLR 381, per Roper J

[99] s. 246(2)

[100] s. 246(3)

The key words of the provision are "maintain the value of assets". It has been commented in submissions to the Minister of Justice[101] that the clause unduly restricts the powers of the interim liquidator, and in particular does not enable the interim liquidator to sell assets which will reduce in value prior to the date of the winding up order. However, in the writer's view the clause does not so restrict the abilities of the interim liquidator. The words "maintain the value" clearly confer the power to sell assets, if doing so will maintain their value. This view is borne out by the words of the Law Commission in its Report[102], which notes: "The use of 'value' clarifies that the liquidator is not required to preserve assets if their value is declining; he or she may, for example, sell perishable goods, thereby preserving their value".

B. Supervision of the Liquidator by Creditors

As discussed above, sections 243 to 245 of the 1993 Act reintroduce the ability of creditors to exercise control over the appointment of the liquidator, and the conduct of the liquidation. The clauses were inserted into the second draft of the Bill after sharp reaction to their absence in the first draft Bill[103] (ref). It is unfortunate that the drafting of these provisions is not particularly clear, and involves references to several other clauses scattered throughout Part XVI of the new Act in order to understand the relatively simple procedure they set out.

In the case of companies put into liquidation by shareholders or the Board (essentially voluntarily) the starting point is a decision as to whether or not the directors can complete a declaration of solvency. The declaration required from the Board under this provision should be easier to satisfy than the declaration required under the 1955 Act. Under present law the directors are required to make a "forecast" of the company's liquidity over the next 12 months[104]; whereas the 1993

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[101] Submission dated 1 March, 1993 from the Society of Accountants and dated 25 February 1993 from KPMG Peat Marwick

[102] Above n.2 para 663

[103] In submissions to the Select Committee

[104] s. 274 Companies Act 1955

Act[105] requires a declaration of its ability to pay debts at one point in time only - at the time the liquidator is appointed. The directors voting in favour of the declaration must certify as to their view and the reasons for it. If such a declaration is made, the liquidator is not required to comply with section 243.

Creditors of a solvent company do not require the protection afforded by the provision where they will be paid out in full. As discussed throughout this paper, the new Act does not consistently carry through the position that creditors of solvent companies in liquidation do not have an interest in the liquidation.

However, section 244 may then assume significance. This is essentially a re-enactment of the present position under the 1955 Act[106], and provides that the liquidator must call a meeting of creditors if he or she discovers that the directors' certificate was not given on reasonable grounds, or that the company cannot pay its due debts.

Where the liquidation is insolvent and commenced "voluntarily", the liquidator must call a meeting of creditors to determine whether to resolve to appoint a new liquidator[107]. The creditors can also determine at that meeting whether to pass a resolution specifying a time or times that creditors' meetings should be held[108].

If the liquidation is court-ordered, the liquidator must call a meeting of creditors to determine whether to apply to court for the appointment of another liquidator. If such a resolution is passed, the first liquidator must then apply to court for an order accordingly[109]. In the writer's view, the need for the liquidator to make an application to court adds unnecessarily to the time and expense of the liquidation, and goes against the thrust of the reforms, which is to simplify the liquidation process. As the Society of Accountants points out in its submission to

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105 s. 243 Companies Act 1993

106 s. 279 Companies Act 1955

107 s. 243(1)(a) Companies Act 1993

108 s. 243(c) and s.258 Companies Act 1993

109 s. 243(7)

the Minister of Justice[110], at present it takes three to four months to get such an application before the court in Auckland.

As with the Companies Act 1955, the fact that not all companies wound up by the Court are insolvent is not addressed in these provisions. Thus, in the case of solvent, involuntary liquidations, creditors are provided with a protection they do not need, and the expense and time of the liquidation is increased accordingly. The fact that all creditors will be paid out would be a factor that a liquidator would be entitled to take into account in deciding whether to call a meeting of creditors; however the creditors retain the ability to insist on the meeting if they so wish[111].

The important exceptions under the 1955 Act to the obligation to call a meeting of creditors are carried through to the Act[112]. In the writer's view this ability of the liquidator to exercise a discretion not to call a meeting is a useful and pragmatic power and, balanced by the ability of creditors to force the liquidator to call the meeting, does not unduly prejudice the interests of creditors.

C. Role of the First Liquidator

In effect then, except in the case of what could be termed a solvent, voluntary winding up, upon appointment the first liquidator takes up the functions presently automatically conferred on the official assignee as provisional liquidator.

It is important to distinguish between a provisional liquidator appointed before the winding up and one appointed upon winding up. The former is replaced in the new Act with an interim liquidator. There is no equivalent in the new Act of the latter.

Although there is clear authority under current law prescribing the role of a provisional liquidator appointed prior to a winding up order,

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110 Dated 1 March, 1993

111 cl. 245

112 s. 245 Companies Act 1993

to the effect that the provisional liquidator in those circumstances must act only so as to preserve the status quo, the writer has been unable to locate any New Zealand authority on how far the official assignee, as provisional liquidator appointed after the winding up order has been made, may go in administering the liquidation.

Under the provisions of the 1993 Act, by the time the creditors' liquidator is appointed under section 243, in the case of a court-ordered liquidation, thirty days may have elapsed, and very possibly it could be a number of months before a second liquidator is appointed; for example if the first liquidator initially sends out notices that he or she does not intend to call a meeting under section 245, and the creditors then require one to be called. The 1993 Act does not restrict the ability of the first liquidator to take steps in the liquidation. By the time the second liquidator is appointed, there may be few or no assets left to administer.

The failure of the new Act to limit the extent of the powers of the first liquidator could give rise to some potentially difficult situations. Take the example of the liquidation of company whose only asset is a restaurant business. If one willing buyer presents itself to the first liquidator after the Court ordered the winding up of the company, the first liquidator is faced with the dilemma of having to decide whether to conclude the sale on the basis that the price offered is the best available, and an opportunity which may not repeat itself; or delaying the sale until the creditors have an opportunity to appoint their own liquidator. If the liquidator takes the first course, he or she may face liability if the creditors and the second liquidator are not in agreement with the sale or its terms. If the liquidator does not proceed with the sale he or she may lose the opportunity to sell at a good price or altogether, given the delay which may occur before the second liquidator is appointed.

If the liquidator were a "tame" liquidator appointed by resolution of the company, it may be that he or she will collude with the shareholders, for example by selling the business to the major shareholder at an undervalue. By the time the creditors' liquidator is appointed, although there is the opportunity to detect the

collusion, the creditors will nevertheless bear the cost of rectifying the situation.

It is suggested that there are two possible solutions to this problem - firstly, the ability of the first liquidator to take major steps in the liquidation could be restricted. This would seem to give meaning to the ability of the creditors to have their own liquidator appointed in the first place. Alternatively, or in addition, the time limit within which the creditors' meeting held under section 243 could be shortened considerably. In relation to Court-ordered windings up it is suggested that there should be no need for the liquidator to have to apply to the Court for the replacement liquidator. Given that the 1993 Act attempts to simplify the procedure and do away with the distinctions between the different sorts of liquidations, there does not seem any good reason why creditors should need to apply to Court in the case of court-ordered liquidations, but not in those which commenced with a resolution of the company. In addition, this contention seems to be supported by the policy of reducing the role of the Court in the case of court-ordered liquidations.

D. The Committee of Inspection

As discussed above, under the 1955 Act, a liquidator may not undertake certain actions without first obtaining the sanction of the court or alternatively, the committee of inspection. Most other jurisdictions surveyed above contain a similar level of supervision by either of those bodies as that provided for in the 1955 Act. The exception is Australia, which nevertheless maintains the need for sanction for major contracts or compromises. The new Act, in its removal of all need for sanctions, is therefore unique, and in the writer's view poses an unnecessary risk to the protection of the rights of creditors of insolvent companies[113], as well as sometimes putting a liquidator in an invidious position[114]. The removal of the need to constantly revert to court, with the time and expense inherent in such applications, will no doubt be welcomed by

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[113] As discussed above, this is not a problem for creditors of solvent companies

[114] As will be discussed in the context of a fact example, below

creditors and liquidators alike. The Law Commission identified the need to constantly revert to court as the single greatest criticism of the current regime[115]. However, removing such protection for creditors can only be justified if more flexible and effective accountability of the liquidator to the creditors is provided for.

It is the writer's view that the provisions of the 1993 Act do not provide watertight protection for creditors. As discussed above, in a large percentage of liquidations where the company is very insolvent, liquidators are permitted not to call a meeting of creditors, and are not obliged to forward an initial report and statement of affairs to creditors[116] . In such situations it becomes advantageous for a liquidation committee to be appointed, in order to ensure that the actions of the liquidator are monitored, and that the rest of the creditors are kept informed. The success of the powers of creditors to prevent or attack an action of the liquidator is dependent on the creditors receiving timely information. The committee or the creditors can then make application to court under sections 284 or 286 of the Act for an order directing a liquidator not to undertake a certain action, or an order in respect of a failure to comply.

However, a liquidation committee has no positive power over a liquidator under the 1993 Act, in the way that it does under the current Act. The liquidator is bound to report to it,[117] but may continue to act against those views in his or her discretion. It is not clear on what basis the committee of inspection has the power of sanction under the current Act - whether in its own right or delegated from the court. It is clear that the Law Commission proceeded on the basis that if the court does not have the power to sanction, then it follows that the committee of inspection cannot hold such power: "The reduced role of the Court also means that committees of inspection, which can be a substitute for the Court (section 240 of the 1955 Act), have a different role".

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[115] Above, n.2 para 624

[116] s. 255 Companies Act 1993

[117] s. 315 Companies Act 1993

However, it can be argued that the absence of a delegating power equivalent to section 266 of the 1955 Act which delegates certain powers of the court to the liquidator indicates that the power to sanction is conferred upon the liquidation committee in its own right. In any event, there is no reason why such power could not be conferred upon a liquidation committee. Very extensive powers are conferred on committees of inspection under US Chapter 11 reconstructions in order to relieve the courts and the other parties involved from the need to obtain sanction from the courts constantly[118]. The ability of the liquidation committee to sanction the more risky actions of liquidators would appear to be one solution to the practical difficulties inherent in applying to court for sanction. In the writer's view the power to sanction is a more effective check on the liquidators' duties than that provided by sections 284 and 286. The balance struck in the Law Commission Bill rested on the one hand on the expertise of an objective and insolvency practitioner. This balance has been removed in the 1993 Act, and in the writer's opinion could be restored by the ability of the creditors to sanction the acts of liquidators. Rights of application to court after the liquidator has acted incur expense, and will rarely restore creditors to the position they would have been in if the liquidator had not acted contrary to their interests.

VI PRACTICAL EXAMPLE

A The Facts

A Limited has been placed into liquidation by way of court order at the suit of the Department of Inland Revenue for non-payment of GST (not a preferential debt) A Limited carried on a tomato dehydrating business. It exported dried tomatoes. A Limited's major asset (in fact virtually its only asset) is a dehydrating machine which it bought from an Australian firm called Dry Out Limited about eighteen months ago. The machine was purchased by way of an agreement whereby A Limited paid a deposit to Dry Out, and the balance (with interest at the

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[118] See Blain and O'Gawa *Creditors' Committees Under Chapter 11 of the United States Bankruptcy Code: Creation, Composition, Powers, and Duties* 1990 Marquette Law Review, p.581

market rate) by equal monthly instalments thereafter. A Limited now has about 70% equity in the dehydrator, although its overall value has depreciated considerably . Dry Out has an Instrument by Way of Security over the dehydrator.

The creditors of A Limited are:

Secured Creditors	(Dry Out)	$100,000
Preferential Creditors	Wages	$15,000
	ACC	$15,000
Unsecured Creditors	(trade creditors and unpaid rental)	$15,000
	(IRD)	$15,000
<u>TOTAL</u>		**$160,000**

The company's assets are:

Miscellaneous chattels	$600.00
Dehydrating machine	$135,000
<u>TOTAL</u>	**$135,600**
<u>SHORTFALL</u>	**<u>$ 24,400</u>**

The realisation of the dehydrator is therefore crucial to the ability of the creditors to obtain any dividend in the liquidation.

A Limited's major shareholder (80%) is B Limited, its other shareholders are its three directors. They are also the directors of B Limited.

B Limited owns the premises from which A Limited operated, and leases them to A Limited. B Limited has not filed a claim in the liquidation, and it appears that A Limited has kept up to date with its rental payments. A Limited also leased a small office from another firm in the city, since its factory premises are a little way out of town. Unfortunately it has fallen well behind on its rent, and in addition it has failed to maintain the office, which was extensively damaged at last year's Christmas party.

B Limited claims that the dehydrating machine is fixed to the land, and is therefore a landlord's fixture, rather than a chattel available in the liquidation. B Limited has erected a fence around the machine so that it cannot be removed. However, it appears to the liquidator from her own observation, and a quick skim through a couple of law books that this claim by B Limited appears to be quite spurious.

B. Meeting of Creditors

Upon appointment by the court, perhaps as a nominee of the petitioning creditor, perhaps from a court list, the liquidator must consider whether to call a meeting of creditors under section 243, and whether to prepare a statement of affairs and initial report under cl 255. The liquidator is required to make a judgement call on this issue. If the major asset of the company in liquidation is recovered, the unsecured creditors are likely to receive well in excess of twenty cents in the dollar, and there would not appear any reason for the liquidator to consider, on the grounds set out in section 245 that no meeting of creditors should be held. On the other hand, if the dehydrator cannot be recovered (remembering that there are insufficient assets in the estate to fund any proceedings), the return to the unsecured creditors will be less than the twenty cents in the dollar mark, and the liquidator may consider that the calling of a meeting of creditors to make an election on the appointment of another liquidator is not justified given the very low level of easily realisable assets in the estate. However, the position is made easier for the liquidator under the new Act than it would be under current law, as she will be entitled to appoint a solicitor early on in order to assess the strength of the company's title to the dehydrator, without the need to obtain sanction of the court or the

creditors to advise on whether or not the major asset of the company in liquidation is recoverable. This will assist the liquidator in forming a view as to the likelihood of succeeding in realising the dehydrator, and thus the feasibility of calling a creditors meeting.

Assuming that the legal advice is that there is an excellent chance of retaining ownership of the dehydrator, the liquidator will probably go ahead and call a creditors' meeting, after first compiling a statement of affairs, an initial report for creditors and settling a list of creditors. However, in the meantime, the liquidator's solicitor is likely to provide legal advice that in order to ensure that the dehydrator is not dealt with by B Limited on the basis of its claimed landlord's lien, it is necessary to apply to court for an order restraining it from so doing until the issue of ownership has been resolved between the parties. The liquidator faces the decision of whether to wait until the creditors have had an opportunity to affirm her appointment, or to seek the appointment of another nominee. In this case, because the order would have the effect of preserving the asset, and thus the status quo, it would be quite proper for the liquidator to go ahead and apply for the order without recourse to the creditors. More difficult for the liquidator would be the decision if an offer to buy the dehydrator were received at this time. Obviously any acceptance of such an offer would have to be conditional on the successful outcome of the challenge to B Limited's claim for a landlord's lien, but given the fact that the market for such machinery is very limited in New Zealand, the first liquidator is placed in a difficult position. In order to protect herself against future claims by the creditors, the liquidator could make an application to court for an order directing her to sell the asset for the price offered. Such an application would need to be supported by a valuation. In that way, both the creditors and the liquidator are protected. However, there is no obligation on the first liquidator to make such an application, since her powers and discretion are not limited in any way, and creditors therefore face the risk of the liquidator dealing with the asset in a manner potentially adverse to their interests, before creditors are fully advised of the facts or have had an opportunity to make their views known.

C. *Secured Creditors*

Assuming that the asset has been preserved by court order, and a creditors' meeting is held, the liquidator (either the liquidator originally appointed by the court or one appointed at the instance of the creditors) must ascertain the position of the secured creditors, Dry Out Limited. The ability of the secured creditor to stand aloof from the liquidation, relied upon by Williamson J in the *Your Size Fashions* decision[119], while it remains in the 1993 Act, has been circumscribed. Under present law, the rights of secured creditors are found under s. 90 of the Insolvency Act (which applies by virtue of s. 307 of the Companies Act). Under section 90, a secured creditor presently has three options:

i. to realise the security, and to prove for the balance; or

ii. to surrender the security and prove for the whole debt, ranking equally with general creditors and losing the right to interest on the debt. There is a right, under certain conditions, to withdraw the surrender, or submit a fresh proof of debt; or

iii. to give an estimate of the value of the security to the liquidator who can pay that value or sell the charged asset and pay the proceeds to the secured creditor. The secured creditor then has the right to prove in the liquidation for any shortfall between the estimated value and the proceeds of sale.

Section 305(1), (2) and (3) substantially carries through this position, and liquidators will no doubt welcome the fact that the provisions are now clearly spelt out in the Companies Act. However, under section 305(8), the liquidator can force a secured creditor to make an election under section 305(1), by serving the creditor with notice that within 20 days of the notification, the creditor must make an election. Failure to do so results in the deeming of the secured creditor to have surrendered the security to the liquidator for the general benefit of all creditors.

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[119] Above, n.80

Section 305(8) represents a marked erosion of the rights of secured creditors. The secured creditor may be forced to take action in relation to the asset within a very short time frame. Conceivably a liquidator could call for an election soon after appointment. A liquidator may well be attracted to clarifying the stance of the secured creditors at the beginning of the liquidation process, in order to plan the progress of the administration of the liquidation. Even though the liquidator is not obliged to settle the list of creditors for up until 30 days after the date the liquidation commenced[120], the identity of the secured creditors is readily available from both the company's list of charges, and from the register of charges on the company's file at the Companies Office[121]. There us nothing preventing the liquidator from serving notice under section 305(8) on the secured creditors before the list of creditors is settled under section 255, or before sending out the report required to be sent to all creditors under section 255(2)(c)(ii). Indeed, the liquidator may wish to force the secured creditors to make the election in order to assist her in compiling the portion of the report relating to proposals for the conduct of the liquidation[122].

The secured creditor may be in the position of having to make an election without the benefit of the liquidator's information as to the state of the company's affairs, some of which may be relevant to which election she may make. For example, a secured creditor who has security over a specialised piece of equipment, which is an integral part of the company in liquidation's operations, and for which there may be little demand on the open market if sold in isolation, may wish to know whether the liquidator proposes to sell all of the plant as a unit, since this may be relevant to the decision whether to leave the asset with the liquidator and claim for its value, or to realise the asset outside of the rest of the liquidation. The ability, in section 305(10), to later rely on the charge, (even in the case of a deemed surrender),

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[120] s. 255 Companies Act 1993

[121] Note that under the previous draft Bill the secured creditors were obliged to notify the liquidator of the existence of a charge, presumably in anticipation of the proposed legislation which it is envisaged will remove the register of company charges from the Companies office; however this requirement was removed in the later draft of the Bill.

[122] Required under s. 255

does not assist the secured creditor who is forced to make an early election, in the absence of all material information, and elects to rely on the charge, and to realise the asset outside of the liquidation, In practice, most secured creditors rely on their charge, but the case of *Your Size Fashions*[123] is an illustration of the fact that this is not always so, even in the case of large, institutional lenders.

The change of the language in clause 268(6) of the second draft of the Bill (which is the direct predecessor of section 305(7) of the 1993 Act) from that of cl 268(7) in the first draft of the Bill is also significant. The first draft imposed, in circumstances when the secured creditor makes a claim, an obligation on the liquidator to redeem, or realise the charge, or to reject the claim. In other words, the liquidator is obliged to take some positive step when a claim is made by a secured creditor. By contrast, section 305(7) in the 1993 Act, based on the later draft of the Bill, imposes no such obligation, but uses the word "may" in respect of redemption, and is silent on the ability of the liquidator to realise the asset. The liquidator is therefore not obliged to take any steps in respect of an asset in relation to which the secured creditor has elected under section 305(1)(b). The effect of this omission renders section 305(1)(b) at best a risky option for secured creditors, in that they have no guarantee that their security will be redeemed, and at worst an expensive waste of time. The expense of obtaining a valuation and perhaps also a revised valuation[124], and the time involved in doing so may fatally affect the secured creditor's ability to obtain value for the asset if the liquidator chooses not to act on the valuation, as she is entitled to do under section 305(7). There is no obligation on the liquidator to give the secured creditor notice that she does not intend to redeem the security. Nor is there a time limit within which the liquidator must make her decision. The clause allows the liquidator to redeem "at any time". In addition, it is unclear whether the secured creditor would be entitled to elect any of the other options described in clause 268(1) in the event that the liquidator chooses not to redeem the security, and practically this may not be possible if the

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[123] Above, n.80

[124] Cl. 305(6)(b)

delay on the liquidator's part is too great. Dry Out Limited should think twice about exercising this option.

Nor is clause 305(7) ideal from the liquidator's point of view. While it gives the liquidator carte blanche to take no action in respect of the claim, if the liquidator decides to take action, the only option available to her is to redeem the security. The option of realising the asset, available under current law [125] and under the provision's predecessor[126] is not carried through to the reported-back version of the Bill. Clause 268(7) of the first draft of the Bill provided:

> Where a claim is made by a creditor as a secured creditor, the liquidator must -
>
> (b) Realise the property subject to the charge and pay the secured creditor the lesser of the amount of the claim and the net amount realised taking into account the liquidator's reasonable remuneration.

The valuation procedure in section 305, based on the amended clause 268 of the second draft of the Bill, with the onus on a liquidator to accept a valuation, places a heavy responsibility on a liquidator, and a commensurate risk on the other creditors of the liquidation. The secured creditor would obviously submit the highest valuation possible, and takes the risk that the valuation is lower than the price he would have received if he had elected to realise the asset himself. That is the risk, it is suggested, which should properly lie with the secured creditor, since other, less risky options are available to him, if he so chooses. If the liquidator accepts a valuation which is too high, and is bound to redeem the asset at that value, the return to the other creditors of the company's estate is reduced by the amount of the excess of the valuation over what the liquidator eventually realises the asset for. To counter this risk, the liquidator would no doubt wish to obtain her own valuation of the asset[127]. Given that the liquidator is unlikely to accept a valuation of the secured creditor which exceeds the liquidator's own valuation, the expense of obtaining two valuations

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[125] s. 90 Insolvency Act 1967

[126] cl. 268(7) of the first draft Bill

[127] the liquidator would no doubt obtain a valuation at some stage of the liquidation in any event, before realising the asset

is pointless. In many cases, the liquidator would prefer to realise the asset[128], and pay the secured creditor the lesser of the valuation or the amount realised. This approach seems fairer to all concerned - it puts the risk on to the secured creditor where it properly lies in this context, and it protects the liquidator and the other creditors of the estate. In this case, given Dry Out's geographical distance from the asset, and the lack of a ready market for it, it is very possible that it will elect to surrender the asset, and claim in the liquidation.

D. Issuing Proceedings

If the secured creditor has surrendered the security, the liquidator must consider issuing proceedings against B Limited for recovery of the dehydrator. The only chance for creditors to receive a dividend in the estate is for such proceedings to succeed. Unfortunately, there is only $600, representing the proceeds of realisation of the company in liquidation's miscellaneous assets, available to fund such litigation. The liquidator must therefore approach creditors to ascertain whether they wish to contribute towards a "fighting fund" for such litigation. It is unlikely that the smaller trade creditors or the Department of Inland Revenue will be willing to contribute to funding the proceedings if Dry Out Limited refuses to contribute also, given that under the pari passu rule, Dry Out will receive the bulk of the any recovery by way of dividend in the estate. If the creditors refuse to fund the proceedings, it is the writer's view that the liquidator is not bound to issue them, no matter what the prospects of success. The creditors have tacitly indicated their agreement to the proceedings not being brought, and although there does not appear to be any authority on this issue, in the writer's opinion, creditors would not succeed in any action for breach of the liquidator's duty under section 253 on such a basis, and that a court would hold the liquidator's failure to bring proceedings reasonable and efficient in the circumstances.

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[128] Remembering that one of the principal duties of a liquidator under s. 253 is to realise the property of the company

The position would be different if it appeared to the liquidator that there was enough money in the estate to bring the litigation. It should be remembered that the decision to issue proceedings often exposes either a liquidator to personal liability for costs, or the estate and thus the creditors if the proceedings are unsuccessful[129]. In general, where an action is to recover a debt, the proceedings should be brought in the name of the company in liquidation[130]. It also appears to be accepted (although there does not appear to have been any judicial consideration of the issue in New Zealand) that in the case of proceedings issues in the name of the company, the liquidator will not be personally liable for costs. In some instances, however, the liquidator must bring proceedings in his or her own name. For example, if the liquidator wishes to recover the rent paid to B Limited, o the basis that it is a voidable preference, and may be attacked under section 292 of the 1993 Act, the application must be made by the liquidator, because of the express wording of the provision: "*on the application of the liquidator*" (emphasis added). It is therefore clear that proceedings issued by the liquidator to recover the rent must be issued in the liquidator's name. In such circumstances, the liquidator faces personal liability for any costs awarded against her, and in practice would seek an indemnity for costs from creditors against such an event.

Because of the lack of available funds in the estate, the creditors in this case appear to be no worse off under the 1993 Act than they would be under current law. This is because the liquidator is forced to consult them on the funding issue, and if issuing proceedings in her own name, to seek an indemnity as to costs. The creditors' protection would be lessened if there were sufficient money in the estate for the liquidator to issue proceedings without recourse to the creditors. In this case the liquidator has obtained legal advice, and has a good chance of succeeding in any proceedings. In other cases, there is nothing to prevent a liquidator from embarking on proceedings in a company's name which are ill-advised and could

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[129] See Hamilton, *Aspects of Official Liquidators' Personal Liability for Costs of Litigation,* Company and Securities Law Journal, August 1989, page 262 and October 1989, page 301

[130] See *Kent & Ors* v *La Communaute de Soeurs de Charite de la Providence & Ors* [1903] AC 220

be costly to the company and ultimately the creditors. Again, it is those more insolvent companies where the liquidator is exempt from the reporting obligations which are most at risk; but even where the liquidator is obliged to report on a six-monthly basis, the creditors may not be informed in sufficient time to prevent such an action on the part of the liquidator. Regular meetings of either creditors or a liquidation committee are the best ways of reducing the risk to creditors. Better still would have been a requirement that the liquidator must obtain sanction of either the liquidation committee, or if there is not one, of a meeting of creditors before launching proceedings in the company's name.

E. Disclaimer

The liquidator will also need to consider whether to disclaim A Limited's lease of the city office, where the rent has fallen well into arrears, and the building has been damaged. Under current law[131], the liquidator would be obliged to seek the leave of the court in order to disclaim the lease, and would need to make application within a strictly prescribed time limit. A court must be satisfied that the property which the liquidator seeks to disclaim is truly "onerous property" within the meaning of the provision[132]. The liquidator is not obliged under current law to give notice of the disclaimer to any party, although a court can impose such an obligation.

Under the 1993 Act[133] the liquidator has a great deal more flexibility. There is no time limit within which she must disclaim the property (unless given notice by an affected party under clause 234A), and there is no need to apply for the leave of the court. As a protection for affected parties, though, the liquidator must give notice within 10 days of disclaiming to any affected party known to her, and such affected persons may either prove in the liquidation or apply to court for an order vesting the disclaimed property in them. In the writer's view, the new provision does not provide the creditor

131 s. 312 Companies Act 1955

132 See *Re Potters Oil Ltd* (1985) 1 BCC 99,384

133 s. 269

who is affected by the disclaimer with the same level of protection that the current provisions do. The liquidator has virtually an unfettered ability to disclaim, so long as the property falls within the definition of onerous property. The discretion of the court to refuse to give leave to the liquidator to disclaim has been removed. However, for the main body of creditors the new provision is beneficial, given the much lower cost and speed to the liquidation of notifying affected parties compared to the time and cost of seeking leave of the court under current law.

VII CONCLUSION

For the reasons outlined in this paper, the writer's conclusion is that, overall, the protection afforded to creditors will be reduced under the Companies Act 1993. The simplification into a single procedure of the processes specifically designed to take the particular circumstances of a liquidation into account (for example its solvency or voluntariness) has resulted in a procedure which is not entirely suitable only any type of liquidation. As has been discussed in the course of this paper, this has given rise to paradoxical results. For example, one of the effects of the provisions is that the more solvent a company is when it goes into liquidation, the greater the duties on the liquidator to keep creditors informed, and to involved in the liquidation process. Conversely, in the case of very insolvent liquidations the provisions of the new Act permit the liquidator to take absolutely no steps in informing and involving the creditors.

In addition, the position of secured creditors, likely to include the large, institutional lenders, has been seriously eroded by the provisions of the 1993 Act, and in particular by section 305.

The goal of simplifying liquidation procedures appears at first glance to be a desirable one, with the resulting reduction in the cost of complying with complex statutory procedures, and the consequentially higher return to creditors. However, there appears to have been little analysis in the reform process of whether the merits of such simplification, and resulting cost savings outweigh the detriment of the

removal of measures designed to protect the interests of creditors. As Jack Hodder pointed out in his address to the Law Conference at the beginning of 1993[134], the hidden costs of such a reform may be great. Large international investors have a choice of jurisdictions in which to make their investments. Given the fact that New Zealand will now offer, relative to the other jurisdictions considered above, relatively little protection to creditors, there is a real risk that such investors will direct their money elsewhere.

Whether the problems identified by the writer in the course of this paper have, in practice, a significant impact on the commercial community remains, of course, to be seen.

[134] Above, n. 4.

APPENDIX I

Figure One

	1987	1988	1989	1990	1991	1992
Court	461	674	1205	1197	1232	1368
Members'	281	524	2751	499	497	380
Creditors'	67	121	201	178	189	182

Note that the figure for Members' Voluntary Windings Up was particularly high in 1989. This was due to a concessional winding up tax provision, introduced that year in order to encourage the winding up of companies that had ceased trading

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