Restructuring & Insolvency 2021 Year In Review

Russell McVeagh

3 March

Introduction of new business continuity test for tax-loss carry-forward rules

A new "business continuity" test for the purposes of New Zealand's tax loss carry-forward rules has come into effect. The new test aims to allow companies to carry-forward tax losses to offset against profits in future years if the underlying business continues, even if the existing shareholder continuity test is breached. The existing shareholder continuity test allows a company to carry-forward its tax losses only if its shareholding remains the same, or at least to the extent of 49%. The new business continuity test would be applied as an alternative in the event that the shareholder continuity test is breached. It is a hybrid of the Australian "same or similar business" test and the equivalent test in the UK, and includes a number of anti-avoidance features. This should be a welcomed change for distressed-stock market participants and alternative capital providers (who may be more inclined to take equity or equity-like interests, which may have been more commercially challenging under the existing shareholder continuity rules). Our observations on the Bill (before it was enacted) can be found here.

31 March

Court of Appeal delivers much anticipated Mainzeal directors' duties judgment

The Court of Appeal provided guidance on two core duties which protect creditors from the risks of insolvent trading. Our observations on the Court of Appeal judgment can be found here and our lessons for directors can be found here. In summary, the Court of Appeal:

- found that the directors had breached s 135 in respect of reckless trading, which was consistent with the High Court. However, in contrast to the High Court, the Court of Appeal found that the breach did not cause loss to Mainzeal; and
- adopted the "new debt approach", where the directors ought to be liable for new obligations entered into from the date of insolvency until the date of liquidation for breaches of the duty in relation to obligations under s 136. This overturned the High Court's novel approach that the entire shortfall to creditors (or "deficiency") is the appropriate starting point.

19 April

RITANZ's survey of restructuring and insolvency experts

- 93% of respondents expect insolvency appointments to rise over the next one to two years.
- Respondents expected the following sectors to be most impacted: Hospitality (90%), Tourism (88%), Retail (82%) and Accommodation (83%).

20 May

Government releases "Wellbeing Budget" but what about Delta?

- Core focuses are welfare and families, health, housing, infrastructure, climate and tourism.
- Net debt $10b lower than forecast in Dec 2020. However, it remains to be seen how the subsequent Delta outbreak has impacted performance against this budget and mid-term forecasting for government spending, net debt, GDP growth and unemployment. Our observations can be found here.

	ACTUAL		FORECAST		
	2019	2020	2021	2023	2025
Govt spending	$87b	$109b	$111b	$115b	$121b
Net debt	19%	26.3%	34%	48%	43.6%
GDP growth	+2.8%	-1.75%	+2.9%	+4.36%	+2.92%

1 June

Construction retentions regime to be strengthened

The Construction Contracts (Retention Money) Amendment Bill proposes amendments to the retention money regime which aim to strengthen and clarify it by (amongst other things) requiring that money be held in a separate trust account in a registered bank in New Zealand or in the form of complying instruments (such as an insurance policy or guarantee). The Select Committee has recommended changes to clarify the Bill and to strengthen the liability regime. The Bill is awaiting its second reading. Our observations on the Bill (in its initial form) can be found here.

10 September

Directors' conduct can breach the Fair Trading Act in addition to Companies Act duties

The High Court has observed here that claims can also be brought against a director of an insolvent company under the Companies Act 1993 and the Fair Trading Act 1986 relating to much the same conduct. That is, falsely representing that the company can and will pay its debts. In a second judgment here the Court:

- left open the question as to whether the award under s 301 of the Companies Act must be paid to the company (rather than the relevant creditor who has brought the recovery proceedings);
- indicated that, as a point of general principle, amounts awarded for the different claims can be cumulative because they respond to different "wrongs"; and
- concluded that the FTA award is to be paid directly to the relevant creditor and the quantum should be reduced to the extent that the creditor recovers amounts paid as a result of the Companies Act liability.

This is a timely reminder for directors that they should be mindful of the representations and assurances that they provide to creditors, particularly in circumstances of uncertain solvency and where there is questionable or contingent stakeholder support.

23 September

Proposed reforms to directors' duties to enable ESG matters to be considered

The Companies (Directors Duties) Amendment Bill proposes an amendment to the Companies Act 1993 to make it clear that, when a director determines what is in the best interests of the company, the director may take into account recognised environmental, social and governance factors. The Bill is awaiting its first reading. Our observations on the Bill (in its initial form) can be found here.

21 October

Restrictions on advisers from taking certain appointments

The Financial Professional Services Trading Advice Transparency Bill proposes to prohibit a professional adviser who recommends the commencement of a liquidation, administration or receivership of a company from subsequently being appointed as the liquidator, administrator or receiver of that company. The Bill follows significant regulatory change in this area in the Insolvency Practitioners Regulation Act 2019, which introduced licensing of insolvency practitioners to the restructuring and insolvency industry and other associated amendments intended to (among other things) enhance professional standards. Our observations on the Bill can be found here.

26 October

The proceedings by the liquidators of the Halifax group in New Zealand and Australia continue

The proceedings by the liquidators of the Halifax group in NZ and Australia for directions regarding the distribution of investor money and property continued, with an appeal by one of the representative investors relating to the date at which investor entitlements should be valued for distribution purposes. Investors held accounts which recorded positions which were not unilaterally closed out on the date of the administration of the Halifax entities in the two countries. The Court of Appeal of New Zealand and the Federal Court of Australia Full Court upheld the first instance decisions of the High Court of New Zealand and the Federal Court of Australia that the date for determining investor entitlements should be the date of the administration of Halifax New Zealand – and not a later date. See our note on the novel trans-Tasman joint hearing here and the Court of Appeal's judgment here. The novel approach to remote hearings, brought about in part by the COVID lockdowns, continued in the appeal courts, with a joint AV hearing between 6 justices on both courts, and counsel presenting remotely.

31 October

The end of hibernation

The business debt hibernation scheme, was introduced in 2020 as a new measure following COVID-19 lockdowns to help businesses manage repayment of their existing debts. The scheme ceased to operate on 31 October 2021. Businesses can no longer apply to enter into business debt hibernation, however this does not impact those businesses already in the scheme. The most recent MBIE impact report, from 30 October 2020, recognised that scheme uptake was low, and our understanding is that this has remained the case throughout 2021.

2 November

COVID rent relief for tenants

New legislation has been passed that implies a clause into leases providing for a "fair proportion" abatement of rent and outgoings in an epidemic. Arbitration is mandatory to settle disputes in relation to this implied clause and enforcement action that is inconsistent with the implied clause is no longer available. This applies to all leases that (a) do not already have an equivalent provision, (b) are in operation at any time between 28 September 2021 and the date the relevant provision is repealed and (c) do not contract out of the implied clause (for leases entered into after 28 September 2021 only). Our observations on the Bill (before it was enacted) can be found here.

6 December

Evergrande and the grand unknown

After months of rumours of liquidity issues at Evergrande, the second largest property developer in China, it appears that it has failed to pay coupon payments on a subsidiary's US$645m 13% bonds and US$590m 13.75% bonds (due on 6 Nov 2021) after the grace period lapsed on 6 December 2021. Fitch has responded by downgrading Evergrande and its subsidiaries to restricted default status. Whilst Evergrande has not yet made an announcement to the HK Stock Exchange, it is understood that this non-payment default may have caused cross-defaults with other series of Evergrande's notes. Evergrande has established a Risk Management Committee to mitigate and eliminate the group's future risks, yet there has been no formal announcement regarding any restructuring proposal. Given the significant volume of global lending to Evergrande and the importance of China to NZ's (and the global) economy, it remains to be seen to what extent the impact of Evergrande's issues will be felt in NZ.

December

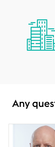
Potential safe harbour reforms in Australia to come

ASIC has now completed consultation on its review of the "safe harbour" protections for company directors from personal liability for insolvent trading if the company is undertaking a restructure. This "fit for purpose" review will also assist the Government to explore further reforms to Australia's insolvency framework to provide businesses with the opportunity to be able to turnaround, restructure and survive. The Treasury paper on the review can be found here and the ARITA submission can be found here. We understand that ASIC should be releasing its report shortly. Industry stakeholders in NZ will no doubt be taking an interest in any developments in Australia to see whether that will influence our Government to consult on directors' duties reforms.

Key trends for next year...

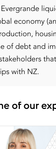
- Implications of the progressive rolling off of remaining government support as we move into the next phase of NZ's COVID recovery and the impact of new COVID variants.
- 2020-2021 have seen creditor forbearance across a range of industries. That will need to be dealt with as and when forbearance and covenant waivers expire, often against the backdrop of increased leverage.
- Disputes as to the "fair proportion" of rent/outgoings to be abated and the impact that those disputes have on the utilisation of cash tied up in those disputes.
- Distressed/opportunistic M&A opportunities for example in the tourism, entertainment, hospitality and adjacent sectors.
- Impact of ongoing supply chain issues globally, but particularly in China, on businesses and prices for consumers (and consequential inflationary pressures).
- Impact of Evergrande liquidity crisis and potential restructuring on the global economy (and in particular, any impact on NZ's primary production, housing and construction industries), given the volume of debt and impact on credit markets, the variety of global stakeholders that could be affected and their various relationships with NZ.

Any questions? Talk to one of our experts



Matt Kersey
+64 9 367 8124
matt.kersey@russellmcveagh.com

Polly Pope
+64 9 367 8844
polly.pope@russellmcveagh.com



Alex MacDuff
+64 (9) 367 8231
alex.macduff@russellmcveagh.com

RMcV