

COMMERCIAL.e.SPEAKING

ISSUE 13 • NOVEMBER 2006

Brought to you by

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Welcome to the final issue of Commercial e.Speaking for 2006. We hope you find the articles both useful and of interest to you. If you would like to see specific business or commercial topics covered in future issues, please get in touch with us. The 14th issue of Commercial e.Speaking will be published in February 2007.

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If you require any further information on any of the topics covered in Commercial e.Speaking, then don't hesitate to contact us. If you do not want to receive this newsletter, please [unsubscribe](#).



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Insolvency Law Reform Bill

- New insolvency and bankruptcy provisions drafted

The Insolvency Law Reform Bill was again reviewed by Parliament in late October 2006, following years of discussion. The Bill will repeal and replace the Insolvency Act 1967, amend insolvency provisions in the Companies Act 1993 and create new legislation on cross border insolvency.

The Insolvency Law Reform Bill provides for:

- * The replacement of personal bankruptcy with streamlining bankruptcy administration and the introduction of the new concept 'no asset' procedure; and
- * The introduction of a voluntary administration procedure for companies with potential for rehabilitation.

What is the 'no asset' procedure?

The 'no asset' procedure (NAP) will be a one-off 12-month alternative procedure to bankruptcy for debtors with total debts of between \$1,000 and \$40,000. A debtor with no realisable assets, who has not been adjudicated bankrupt and has not been admitted to the NAP previously will be able to apply to the Official Assignee for entry to the scheme.

Once admitted to the NAP scheme the debtor will enjoy a debt moratorium. If the NAP runs for 12 months the debtor will be discharged and the debts cancelled. If the NAP terminates at any time before 12 months is up, the debtor's debts will become enforceable. The NAP will be terminated at the request of the debtor if the Official Assignee is satisfied that through change in circumstances the debt or can repay something towards their debts.

What is 'voluntary administration' for companies?

For insolvent companies with potential for rehabilitation, the court or secured creditors will be able to place a company into voluntary administration and appoint a voluntary administrator. The voluntary administrator will manage the company, organise creditors' meetings and draw up a restructuring plan.

Once a company is in voluntary administration creditors will have the opportunity to vote on whether the company should be restructured or placed in liquidation.

At present the Inland Revenue Department (IRD) has priority over other creditors in receiving payment first. Given that the creditors vote on the outcome of a company, the IRD will be inclined to evaluate its recovery out of voluntary administration against its recovery out of liquidation.

If a company is placed into liquidation the IRD has first priority before other unsecured creditors, therefore the IRD would almost always vote in favour of liquidation. For the voluntary administration procedure to be effective all creditors will need to be treated equally and paid out in accordance with the pari passu principle (which provides that all creditors in a class are treated equally). If the IRD remained with its special priority this would defeat the purpose of a company having the right to voluntary administration as the IRD would never agree to it.

Summary

Voluntary administration has the potential to be beneficial to companies in financial trouble, however will only be effective if the IRD's priority is curtailed.

The legislation will not be implemented until regulations are put in place. To date there has been overwhelming support for the establishment of a regulatory framework for the new insolvency provisions.

Submissions on the Bill close on Friday, 2 February 2007. If you would like to make a submission and would like some help with this, please contact us.

Fighting the Fakes - Border patrol

Counterfeiting is now occurring on a massive global scale. Estimated to make up 10% of total worldwide trade, counterfeiting is worth US\$500-US\$700 billion per year. The impact of counterfeiting on business is clearly significant. This article examines what businesses can do to protect their legitimate goods.

A 'counterfeit' is an almost identical copy of a product. Pirated goods are also copies, but not usually exact copies. 'Piracy' is a term usually used to describe DVDs and CDs. The packaging usually makes it obvious to consumers that the goods are not genuine.

The New Zealand situation

New Zealand is only a small country and the release of counterfeit goods here results in a substantial loss of profits for rights holders, and significantly damages their goodwill and reputation. It also threatens the commercial viability of legitimate New Zealand businesses as they struggle to compete with discount stores or markets selling fakes.

There has been a huge increase in counterfeit goods imported into New Zealand over the past five years. Counterfeiters target all sectors, but the major problem areas are clothing, footwear, cosmetics, perfume and children's toys.

Counterfeiting is no longer the sole domain of expensive luxury goods. Today everyday products such as car parts, mobile phones and batteries are copied creating safety hazards for consumers. The quantity of CDs and DVDs seized in recent months has significantly reduced. Downloads now make up the main source of movie and music piracy in New Zealand.

Counterfeit goods are generally found at markets and low-end retail shops, although there have been several cases of counterfeits sold in high street stores.

What can be done to stop counterfeit goods entering New Zealand?

Border control remains New Zealand's main weapon against counterfeit goods because most of these goods are not manufactured here and must enter the country from overseas.

For this reason, the most effective and cost efficient method to stop counterfeit goods is to prepare and file a Customs Notice with the New Zealand Customs Service. Customs has stopped over one million counterfeit items from entering New Zealand since the Notice system was introduced just over 10 years ago.

Customs may only detain counterfeit goods if a brand owner has lodged the required documentation; a Customs Notice and supporting evidence of rights. A Notice can be lodged for a registered trade mark and/or a copyright work.

Customs Notice procedure

The Notice requests that Customs detains any products that come into its possession bearing the same or similar trade mark covered by the Notice or infringing the copyright work. Once a Notice is in place, Customs will detain any goods it suspects of infringing the trade mark or copyright.

Often, an importer will agree to forfeit its shipment immediately and those that don't will generally forfeit on receipt of a strongly worded lawyer's letter. If the importer does not agree to forfeit the goods, the owner of the trade mark and/or copyright work has 10 days to get the importer to forfeit the goods or to decide whether or not it will sue.

Most customs actions settle quickly with the importer agreeing to allow destruction of the goods. In addition, they will usually provide rights holders with their supplier information, appropriate undertakings and, in many cases, a contribution to their legal costs.

Lodging a Notice with NZ Customs is a relatively simple and cost effective way to stop counterfeit or pirated copies of your product from entering New Zealand. If you are concerned that your brand or copyright work may be the target of counterfeiting or piracy then you should ensure that the relevant Notices are lodged with Customs right away.

Structuring Business Equity Funding

- Partnerships and company structures

When establishing or acquiring a business, one of the most important decisions to be made is how the business equity funding should be structured. This article examines some of the issues around a partnership or company structure.

Partnerships

Partnership Agreement

If the partnership model is chosen as the business entity, it is essential that a partnership agreement is drawn up. Many spousal partnerships (including married, de facto and same sex spouses) do not bother with a formal partnership agreement. However, it is clear that there are benefits from having an agreement as opposed to relying on the default option, provisions for which are contained in the Partnership Act 1908 (PA). With the PA remaining virtually unchanged for 98 years, many of its provisions do not suit today's business environment.

Capital

Section 27 of the PA provides that no interest is payable on agreed capital contributed. However, interest at 5% is allowed on capital contributions in excess of the agreed capital, for example, a loan to the partnership. The Inland Revenue Department (IRD) treats any interest payments on agreed capital as a distribution of profits and will not allow a deduction to the partnership. Interest deduction is allowed for loans.

Unless a partnership agreement provides otherwise, equal profit sharing is mandatory under the PA. If, for example, there is an unequal labour contribution, the only way to recognise that financially in absence of an agreement, is to have an employment agreement and pay the relevant PAYE deductions.

Another matter that should be addressed in a partnership agreement is that under the PA, upon dissolution of the partnership, the capital is divided in proportion to the profit sharing ratio and not the actual balance. If one partner has had higher drawings than the others and their capital account balance is lower, then without a contrary provision in an agreement, the unequal balances will not be recognised. There is no distinction in partnerships between a partner's capital and current accounts. Under the PA it is all lumped together as equity, unless otherwise provided for in a partnership agreement.

Companies

Equity funding in most companies has historically been a small amount of subscribed share capital with the greater proportion attributed to shareholder loans. This facilitated the payment of interest on the loans rather than having to rely on dividends for distribution of profits.

Tax

In general terms the tax position is:

- Where shareholder loans are proportionate to the shareholding, the Income Tax Act treats the loans as equity and not debt.
- Where shareholder loans are interest free upon demand and interest is demanded and paid on loans at less than commercial rates, the Income Tax Act does not allow a deduction to the company.
- Where a shareholder has borrowed funds to enable them to lend the funds to the company, current tax rules do not allow a loss to be claimed by the shareholder. Deduction is limited to the amount of income received from the company, so it can only ever be a neutral position.

Shareholders' Agreement

In addition, a comprehensive shareholders' agreement should also be entered into so that the terms of any shareholders' loans, dividend policy, drawings policy, exit and entry rules, pre-emptive rights on shares, and dispute resolution procedures (plus a range of other issues) can be clearly set out and agreed upon.

Business Briefs

Business redeploys to internet

Some recent indications of current trends:

- **Real estate:** Trade Me has accused www.realestate.co.nz (the Real Estate Institute's website) of misleading advertising to promote itself as the country's leading property website. The Advertising Standards Authority is considering the matter after Trade Me filed a complaint in August. Realestate.co.nz calls itself the 'most popular dedicated property website' and 'the only place with every place'. Trade Me's property section attracted nearly 400,000 visitors in September, more than realestate.co.nz's 160,000.
- **Trade finance:** Finance company G E Money has completed a deal with Trade Me to provide online finance for its vehicle listing site, Trade Me Motors. G E Money claims the deal effectively corners the online vehicle finance market.
- **Antique dealers:** A Palmerston North antique and second-hand dealer claims more and more people are using Trade Me to buy and sell goods, forcing many second-hand dealers to close. Fred Ramsay of Paddington Station and The Old Country Furniture Store said, "We just don't get the people to our store. People would rather just stay home and trawl Trade Me."

Failures to get negligence remedy where there is no contractual nexus

Two recent cases demonstrate the difficulty of obtaining negligence remedies in a contract environment:

- *Carter Holt Harvey Ltd v Genesis Power Ltd (No 4) 24/10/06, Randerson J, HC Auckland CIV-2001-404-1974*

Rolls-Royce New Zealand was able to strike out part of Carter Holt Harvey's Statement of Claim in respect of construction and operation of its cogeneration plant in accordance with contracts between Carter Holt and Genesis Power, and Genesis Power and Rolls Royce.

Carter Holt claimed Rolls Royce owed it a duty of care, based on a purported special relationship arising out of pre-contractual dialogue and that this duty of care was beyond liability for negligent misstatement. Justice Randerson held that the complex contractual arrangements between the parties was evidence of an intention that relationships be governed by contract and that accordingly Rolls Royce assumed responsibility to Genesis Power only (no direct contract link with Carter Holt).

- *Prime Commercial Ltd v Wool Board Disestablishment Company Ltd 18/10/06, CA110/05*

Prime Commercial entered into a tender process to buy the Wool Board's building. The Wool Board sold to another purchaser, from whom Prime Commercial subsequently purchased at higher price. The Court of Appeal held that there was no 'process contract' in the tendering process and that there was no basis for misrepresentation. Prime Commercial's attempt to use tort of negligence to make up for lack of process contract was rejected on policy grounds.

General Security Agreement prevails

Harvest Pro Logging Limited v Cordyline Holdings Limited 3/10/06, Associate Judge Doogue, Auckland High Court.

Cordyline Holdings had entered into an agreement for sale of four logging trucks and trailers to Forestone; Forestone subsequently defaulted on payment and ceased trading. Harvest Pro Logging held a General Security Agreement (GSA) over Forestone's property and gave notice to Forestone of its intention to take possession of Forestone's assets.

Before becoming aware of the Harvest Pro Logging GSA, Cordyline disposed of the vehicles pursuant to purported continued ownership under the sale agreement. The decision gave precedence to Harvest Pro Logging's GSA under which Harvest Pro was entitled to immediate possession of the vehicles at the point when Forestone fell into arrears under its GSA and ceased trading.

Cordyline's ownership of the vehicles ceased at the point its sale contract with Forestone became unconditional, so its subsequent taking of possession interfered with Harvest Pro's prior rights to possession under its GSA. Judgment was given against Cordyline for \$980,000.