

# Financial Services Quarterly

WINTER 2006

Bell Gully





**Welcome to the Winter 2006 issue of *Financial Services Quarterly*, a review of current legal issues in the financial sector.**

Each quarter, we summarise recent issues and preview upcoming developments under these headings:

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- **Changes to NSW stamp duty laws**
- **Anti money laundering reforms open for discussion**



**Need more information?**

For more information on any of the cases, articles and features in *Financial Services Quarterly*, please email [rachel.gowing@bellgully.com](mailto:rachel.gowing@bellgully.com) or call on 64 9 916 8825.

*Disclaimer: this publication is necessarily brief and general in nature. You should seek professional advice before taking any action in relation to the matters dealt with in this publication.*

## In the courts

### **Liquidator not a third party for the purposes of the PPSA**

A liquidator has been held to be an agent of the debtor company and not a third party, meaning that an unsigned retention of title document can be enforceable against a liquidator if it creates a security interest, even though it does not meet the requirements of the Personal Property Securities Act.

### **Electronic funds transfer good payment**

The Court of Appeal has determined that a payment by electronic funds transfer is equivalent to payment by bank cheque.

### **Deed enforceable by third party if intended**

An English court has found that a guarantee entered into as a deed between the principal debtor and the guarantor, but not executed by the creditor, was nonetheless enforceable by the creditor.

### **Declaration of trust over the benefit of contractual rights not effective to entitle beneficiary to enforce those rights**

An English court has decided that it is not possible to circumvent a provision in a facility agreement prohibiting assignment by a lender by the use of a declaration of trust.

## In the journals

### **Trans-Tasman mutual recognition of securities offerings**

This article identifies impediments to advancing mutual recognition of securities offerings in New Zealand and Australia due to the differing disclosure requirements in each country.

### **Reducing regulatory burdens on financial services businesses**

The Taskforce on Reducing Regulatory Burdens on Business (an Australian Government taskforce) produced a report in April 2006 identifying key areas of concern relating to over-regulation. This article focuses on the issues that were raised for the Australian financial services industry.

## Legislation/In Parliament

### **Proposed tax changes for limited partnerships**

New rules on limited partnerships have been proposed to attract more venture capital investment into New Zealand.

### **Update on Securities Legislation Bill and regulations**

The Securities Legislation Bill is being held up while a Supplementary Order Paper is being put together to address concerns that have been raised in public submissions.

### **Insolvency law reform - update**

The Government's decision to grant the IRD preferential creditor status, allowing it to block a request for voluntary administration, is being questioned.

### **Anti money laundering reforms open for discussion**

A discussion document on enhancing measures to counter money laundering and the financing of terrorism has been released.

## Recent developments

### **Changes to NSW stamp duty laws**

Limiting the amount recoverable under a security document may no longer be effective to cap the amount of stamp duty payable in New South Wales.

### **Directors' and officers' disclosure review**

A review of the directors' and officers' disclosure obligations in the Securities Markets Act has been announced.

### **Financial intermediaries discussion paper released**

A discussion paper on the co-regulatory model for financial intermediaries was released in early July. The Ministry of Economic Development is now seeking industry feedback, and has acknowledged concerns about the costs of the new regulatory framework.

## In the courts

### Liquidator not a third party for the purposes of the PPSA

*A liquidator has been held to be an agent of the debtor company and not a third party, meaning that an unsigned retention of title document can be enforceable against a liquidator if it creates a security interest, even though it does not meet the requirements of the Personal Property Securities Act.*

In this case<sup>1</sup>, goods were supplied under terms and conditions of trade set out in the supplier's standard invoices. The invoices incorporated a retention of title in, and a security interest over, the supplied goods. The purchaser didn't sign the invoices – indeed there was no signed agreement between the two parties.

The supplier registered a financing statement on the Personal Property Securities Register for the supplied goods and its purported security interest over them.

When the purchaser got into financial difficulty, liquidators were appointed and the supplier asked them to return the goods. The liquidators refused, sold the goods and refused to apportion any of the proceeds in the supplier's favour.

When the supplier applied to the High Court for summary judgment against the liquidators for conversion, the liquidators argued that because the parties did not have a signed agreement, the supplier's purported security interest was not enforceable against it under section 36(1) of the Personal Property Securities Act 1999 (the PPSA). Section 36(1) provides that a security interest must be evidenced in writing if it is to be enforceable against third parties. A security interest is enforceable between the parties whether it is in writing or not.

The court decided that the supplier did have a security interest, and that it was binding on the liquidators. The decision was reached on the basis that section 36(1) of the PPSA was not relevant because this section relates to the enforceability of the security agreement between the debtor and a third party. On these facts, the liquidators were not a third party of the debtor – they were its agent.

The liquidators were ordered to pay the value of the supplied goods, together with interest.

Notwithstanding the outcome of this case, the best protection for a financier or supplier is always to ensure that a security agreement, incorporating an adequate description of the collateral, is signed by the parties, and that the interest is registered on the PPSR. This applies for all types of security interest, including retention of title arrangements.

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<sup>1</sup> *Sleepyhead Manufacturing Co Limited v Dunphy* (2006) 9 NZCLC 264,000 and 20-280

## Electronic funds transfer good payment

*The Court of Appeal has determined that a payment by electronic funds transfer is equivalent to payment by bank cheque.*

In this case<sup>1</sup>, the vendor of some residential units served a settlement notice on the purchaser for failing to settle by the agreed date. The vendor's solicitor had specified that the settlement was to be completed by the purchaser depositing a bank cheque into its trust account along with fax confirmation. The agreement provided that a working day ended at 5pm.

At 4.54pm on the last day for settlement, the purchaser's solicitor deposited the settlement funds by electronic transfer into the vendor's solicitor's trust account. The vendor's solicitor's fax machine was engaged, and the fax confirmation couldn't be sent through at that time. At 5.03pm, the vendor's solicitor sent a fax to the purchaser's solicitor cancelling the agreement.

The court decided that payment by electronic funds transfer was acceptable because this method can be equated with bank cheques and is a common form of payment. Because the transfer was effected before 5pm, the purchaser had complied with the agreement for sale and purchase.

The court further determined that, as fax notification was not expressly required to have been made by 5pm (only payment was required by 5pm), failure to give the notification by that time did not breach the agreement.

Accordingly, the vendor was not entitled to cancel the contract.

The Supreme Court has granted the vendor leave to appeal on the question of whether the purchaser was entitled to use electronic funds transfer as a method of payment and whether payment was received in time, notwithstanding the vendor did not receive the fax notification until after 5pm.

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<sup>1</sup> *Rick Dees Limited v Larsen* (2006) 5 NZ ConvC 194, 256 and 76 - 500

## Deed enforceable by third party if intended

*An English court has found that a guarantee entered into as a deed between the principal debtor and the guarantor, but not executed by the creditor, was nonetheless enforceable by the creditor.*

In this case<sup>1</sup>, the vendor of shares sought to enforce a guarantee given to secure payment of the purchase price, even though the vendor was not a party to (and did not sign) the guarantee. The guarantee was expressed as a “deed” entered into “between” the principal debtor and the guarantor.

The court discussed the distinction between a deed, which confers rights on persons who are not parties to it (a deed poll), and a deed that is enforceable only by the persons who enter into it (a deed inter parties). The conclusion was that it is necessary to consider not just whether one or two persons executed the document, and not just whether the word “between” appears, but also to examine what the parties intended. It may be the case that the parties only made promises between themselves or it may be that they sought to use the document as a means to make promises to a third party.

In this case, the vendor was granted summary judgment on the basis that the guarantee was a type of deed that was not merely intended to create rights enforceable by the creditor, but which in law achieved that intention.

In New Zealand, we recommend inclusion of a clause under the Contracts (Privity) Act 1982, providing that the agreement is enforceable by the party notwithstanding it may not be signed by that party.

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<sup>1</sup> *Moody v Condor Insurance Limited* [2006] 1 All ER 934

## **Declaration of trust over the benefit of contractual rights not effective to entitle beneficiary to enforce those rights**

*An English court has decided<sup>1</sup> that it is not possible to circumvent a provision in a facility agreement prohibiting assignment by a lender by the use of a declaration of trust.*

In the 1980s, the Bank of Zambia entered into an oil import facility agreement as borrower. Clause 12 of the agreement prevented the lenders from assigning their rights other than to a financial institution and with the prior written consent of the borrower. Consent was not to be unreasonably withheld and was deemed to have been given where no reply was received from the borrower within 15 days of a request.

One of the lending banks subsequently assigned its rights to Bank of America in the late 1990s, but the Bank of Zambia did not consent to this and was deemed to have given consent pursuant to clause 12. Bank of America then sold its interest in the debt to a party that was not a financial institution, again without the consent of the Bank of Zambia, but first entered into a declaration of trust over its interest in favour of the assignee.

It was submitted that the declaration of trust put the claimant in the position of Bank of America in terms of its rights against the Bank of Zambia. However, the court had some concern about the use of a declaration of trust to circumvent clause 12.

Ultimately, it was found that the commercial purpose of clause 12 was to ensure that the original parties to the facility agreement were not brought into direct contractual relations with third parties other than as expressly permitted by the provision, and so the assignee was unable to enforce rights directly against the Bank of Zambia.

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<sup>1</sup> *Barbadois Trust Company Limited v Bank of Zambia* [2006] EWHC 222 Comm

## In the journals

### **Trans-Tasman mutual recognition of securities offerings**

**Gordon Walker and Mark Fox, *Company and Securities Law Journal*, Volume 24, Number 4, June 2006**

*This article identifies impediments to advancing mutual recognition of securities offerings in New Zealand and Australia due to the differing disclosure requirements in each country.*

The New Zealand and Australian Governments signed a treaty in February 2006 that is intended to remove unnecessary regulatory obstacles to trans-Tasman securities offerings.

There are currently arrangements in place to facilitate the agreement. For example, an exemption notice under the Securities Act 1978 (New Zealand) allows Australian issuers who are looking to offer securities in New Zealand to avoid New Zealand's registration requirements. Similarly, Australia has a recognition regime under which a New Zealand registered prospectus could be recognised in Australia for the purposes of its Corporations Act 2001 (Cth).

The authors consider that there are problems in taking the mutual recognition initiative any further, primarily because there are significant differences in the disclosure requirements for the two jurisdictions.

Their first example is section 33 of the Securities Act (New Zealand), which prohibits offers of a security "to the public" without a registered prospectus or investment statement. In Australia, it is much clearer when the disclosure requirements of the Corporations Act must be met: unless section 708 says otherwise. So there is the possibility of an offer requiring disclosure under one jurisdiction and not the other.

Their second example is, even if a particular offer requires disclosure under both jurisdictions, the prospectus content rules differ. The disclosure obligations under Australian law are more onerous than those under New Zealand law. This could result in a New Zealand registered prospectus not having sufficient content to comply with Australian law.

The authors argue that to preserve Australia's higher disclosure standards, New Zealand's standards need to be brought into line with those of Australia.

## **Reducing regulatory burdens on financial services businesses**

**Richard Batten, Australian Corporate News, Issue 10, 14 June 2006**

*The Taskforce on Reducing Regulatory Burdens on Business (an Australian Government taskforce) produced a report in April 2006 identifying key areas of concern relating to over-regulation. This article focuses on the issues that were raised for the Australian financial services industry.*

The significant concern was the cost of compliance, in both financial and management resource terms. The taskforce noted that compliance with the current regulatory framework can occupy up to 25% of the time of senior management. This is largely because the Australian Prudential Regulation Authority and the Australian Securities and Investment Commission tend to take an overly rigid approach to regulation.

The taskforce also suggested a number of ways that the Government could improve the existing legislation and ways that they could make laws in the future, which would include a more comprehensive consultation process.

## Legislation/In Parliament

### **Proposed tax changes for limited partnerships**

*New rules on limited partnerships have been proposed to attract more venture capital investment into New Zealand.*

The New Zealand Government has proposed new limited partnership rules, with separate legal entity status and partnership tax treatment, to encourage venture capital investment into New Zealand.

Limited partnerships are an internationally preferred vehicle for investment into a foreign country for the following main reasons:

- they allow investors to limit their exposure to liability to the amount of their investment; and
- they provide a flow-through tax mechanism in respect of gains and losses.

New Zealand currently has special partnership rules in place. However, the rules are recognised as being outdated and restrictive. Of particular concern is that the absence of separate legal personality could render a partner personally liable. The proposed rules will recognise a limited partnership as a separate legal entity.

The new rules will apply to a raft of business activities operating in partnership form, including:

- small, closely-held businesses;
- small, medium and large professional practices;
- small investment activities;
- widely-held investment activities; and
- all sectors, including agriculture, forestry and manufacturing.

Proposed rules for limited partnerships include the introduction of loss limitation rules to ensure that net losses claimed by a limited partner reflect the actual level of that partner's economic loss.

A Bill is expected to be introduced into Parliament next year, with application from the 2008–2009 income year.

## **Update on Securities Legislation Bill and regulations**

*The Securities Legislation Bill is being held up while a Supplementary Order Paper is being put together to address concerns that have been raised in public submissions.*

The concerns include:

- investment advisers might not always be able to meet their disclosure obligations if they have to make all the disclosure prior to giving advice;
- the requirement that investment advisers disclose whether they have been the subject of an adverse finding by a tribunal or disciplinary body could be too broad; and
- professional advisers such as lawyers, accountants and investment advisers may inadvertently be caught by insider trading laws when acting in their professional capacity.

The Supplementary Order Paper is being drafted so that it can go through to the committee stage with the Bill.

In the meantime, the Ministry of Economic Development is preparing a policy paper for Cabinet dealing with investment advisers' and brokers' disclosure, substantial security holders' disclosure, insider trading exemptions and market manipulation exemptions.

## **Insolvency law reform - update**

*The Government's decision to grant the IRD preferential creditor status, allowing it to block a request for voluntary administration, is being questioned.*

A fundamental aspect of the Insolvency Law Reform Bill is the introduction of a voluntary administration regime, which will allow a company in serious financial difficulty to have its debts effectively frozen while the company is managed by an outside administrator. The intention is to give the company an opportunity to nurse itself back to health without being subject to enforcement actions from creditors.

The select committee has received a number of submissions. Of particular interest, the New Zealand Bankers' Association and other parties recommended abolishing the Inland Revenue Department's preference/priority on liquidation. They concluded that this was a significant impediment to the effective management of distressed debtors. The submitters recommended that the IRD put in place incentives that prevent directors from getting to a level of irreversible debt, to protect personal liability. It was noted that both Australia and the United Kingdom have abolished the IRD priority on liquidation, because it operated as a disincentive for the commissioner to recover debt in a commercial manner.

They also noted that the current Bill did not contain a sufficient amount of inter-relation between insolvency matters and the Personal Property Securities Act.

The closing date for submissions on the Bill was 7 April 2006 and it is currently with the Commerce Select Committee. Its report is expected in August.

## Anti money laundering reforms open for discussion

*A discussion document on enhancing measures to counter money laundering and the financing of terrorism has been released.*

The document, which marks a second consultation round, proposes regulatory changes to enable New Zealand to comply with the Financial Action Task Force (FATF) - an inter-governmental body that sets international standards for combating money laundering and terrorist financing. Most of New Zealand's anti money laundering/countering financing of terrorism legislative requirements are contained in the Financial Transactions Reporting Act 1996 (the FTRA). This Act pre-dates the current FATF standards and is deficient in some areas. New Zealand is due for evaluation by the FATF in 2008.

Proposals to address deficiencies in the FTRA include:

- extending coverage of the FATF requirements to groups outside the core financial sector (i.e. to include other professions where laundering could occur, for example lawyers and accountants);
- more stringent checks on customer identity and verification;
- more detailed record keeping and reporting requirements; and
- increased monitoring of compliance with the FATF requirements.

For a copy of the document *Anti-Money Laundering and Countering the Financing of Terrorism: New Zealand's Compliance with FATF Recommendations*, visit [www.justice.govt.nz](http://www.justice.govt.nz). Submissions close on 31 July 2006.

## Recent developments

### Changes to NSW stamp duty laws

*Limiting the amount recoverable under a security document may no longer be effective to cap the amount of stamp duty payable in New South Wales.*

Changes to the stamp duty laws of New South Wales may impact on the amounts of stamp duty payable by parties to transactions with a New South Wales connection.

#### *The changes*

Historically, where advances were secured against property of the borrower located in New South Wales, the amount recoverable under the security could be limited by contract, which effectively capped the amount of the stamp duty payable.

The changes mean that now stamp duty may be calculated on the facility limit, regardless of the amount actually recoverable under the security.

#### *Existing facilities*

The changes could affect any funding that occurs after 1 July, including under facilities that were in place prior to that date.

#### *Impact*

We are unsure at this stage how far-reaching the impact will be, but if you have any concerns about existing facilities, or proposed facilities, we would be happy to assist.

Contact [Murray King](#) or [David McPherson](#).

## **Directors' and officers' disclosure review**

*Review of the directors' and officers' disclosure obligations in the Securities Markets Act has been announced.*

The Government has received feedback from the market that disclosure obligations are harder for companies to comply with than was originally anticipated, particularly with officer disclosure. A review has been announced to see if it can lighten that burden.

Policy proposals will be announced after consultation with the industry. Discussions will also be held with the Australian Government, which is also reviewing this area of the law.

## Financial intermediaries discussion paper released

*A discussion paper on the co-regulatory model for financial intermediaries was released in early July. The Ministry of Economic Development is now seeking industry feedback, and has acknowledged concerns about the costs of the new regulatory framework.*

In December 2005, Cabinet agreed in principle to the adoption of a co-regulatory model that had earlier been recommended by the Task Force on the Regulation of Financial Intermediaries (*as noted in the Spring 2005 FSQ article "Changes ahead for brokers and other financial intermediaries".*) The co-regulatory model requires the engagement of both the Government (through the Securities Commission in particular) and approved professional bodies in order to improve consumer protection in the area of financial advisory services.

Feedback is being sought on:

- who is a financial intermediary, what are the different levels of financial intermediary, and which types of advice and services will be covered by the new regime;
- the conduct and disclosure standards for financial intermediaries; and
- the co-regulatory model, including the powers of the Securities Commission, the powers of the Minister, and the powers and rules of the approved professional bodies.

Submissions close on the 1 September 2006, and final policy decisions will be presented to Cabinet later in the year. The Government is also carrying out a broader review of financial products and providers.

To read an article by David Craig, Partner and Jonathan Norman, Solicitor (both of Bell Gully), titled *New Zealand's Financial Sector Set for a Shake-up* visit: [www.bellgully.com/resources/resource\\_00655.asp](http://www.bellgully.com/resources/resource_00655.asp)

For more information, visit the Ministry of Economic Development's website: [www.med.govt.nz](http://www.med.govt.nz).

## Bell Gully news

### **Mergers and acquisitions market remains strong**

Merger and acquisition activity has continued its domination of the business landscape in the first half of 2006. Figures released by Thomson Financial show that 125 transactions having a value of NZ\$5.4 billion were completed in New Zealand in the first six months of this year, a 52% increase on the same period last year. Thomson's results again place Bell Gully as the top ranked New Zealand law firm advising on M&A deals. In the first six months of 2006, the firm advised on 30 transactions with a total value of NZ\$1.88 billion.

### **Bell Gully leads New Zealand in *Who's Who Legal 2006***

Bell Gully has topped the New Zealand lawyer rankings in *Who's Who Legal 2006*. The International Who's Who of Business Lawyers publication features leading legal practitioners in 27 distinct areas of practice in the international legal marketplace. It is published annually by London-based Law Business Research Limited. Bell Gully consistently ranks as New Zealand leader in the annual Who's Who listings.

### **Boston, London and back to Bell Gully**

Rachel Paris has returned to law firm Bell Gully as a senior associate after four years working and studying in the US and UK. Beginning her career with Bell Gully's banking and finance team, Rachel left to join Harvard Law School's Masters in Law programme. One of only 12 students selected for its International Finance programme, Rachel's study also featured media and entertainment law.

**For further details and more news visit: [www.bellgully.com](http://www.bellgully.com)**

## Useful Web links

### *New Zealand government*

- Consumer affairs [[www.consumeraffairs.govt.nz](http://www.consumeraffairs.govt.nz)]
- Inland Revenue Department [[www.ird.govt.nz](http://www.ird.govt.nz)]
- Ministry of Economic Development [[www.med.govt.nz](http://www.med.govt.nz)]
- Ministry of Foreign Affairs and Trade [[www.mfat.govt.nz](http://www.mfat.govt.nz)]
- New Zealand Government [[www.govt.nz](http://www.govt.nz)]
- NZ Government E-Commerce Information [[www.ecommerce.govt.nz](http://www.ecommerce.govt.nz)]
- NZ Treasury [[www.treasury.govt.nz](http://www.treasury.govt.nz)]
- Office of the Clerk of the House of Representatives [[www.clerk.parliament.govt.nz](http://www.clerk.parliament.govt.nz)]
- Parliamentary Counsel Office [[www.pco.parliament.govt.nz](http://www.pco.parliament.govt.nz)]

### *New Zealand financial agencies and organisations*

- Commerce Commission [[www.comcom.govt.nz](http://www.comcom.govt.nz)]
- The Companies Office [[www.companies.govt.nz](http://www.companies.govt.nz)]
- Export Credit Office [[www.treasury.govt.nz/exportcreditoffice](http://www.treasury.govt.nz/exportcreditoffice)]
- NZ Law Commission [[www.lawcom.govt.nz](http://www.lawcom.govt.nz)]
- Office of the Banking Ombudsman [[www.bankombudsman.org.nz](http://www.bankombudsman.org.nz)]
- Office of Insurance and Savings Ombudsman [[www.iombudsman.org.nz](http://www.iombudsman.org.nz)]
- Office of the Privacy Commissioner [[www.privacy.org.nz](http://www.privacy.org.nz)]
- Personal Property Securities Register [[www.ppsr.govt.nz](http://www.ppsr.govt.nz)]
- Reserve Bank of New Zealand [[www.rbnz.govt.nz](http://www.rbnz.govt.nz)]
- Securities Commission [[www.sec-com.govt.nz](http://www.sec-com.govt.nz)]
- Takeovers Panel [[www.takeovers.govt.nz](http://www.takeovers.govt.nz)]

### *New Zealand commercial sites*

- CLANZ [[www.clanz.org](http://www.clanz.org)]
- Financial Services Federation [[www.fsf.org.nz](http://www.fsf.org.nz)]
- Institute of Chartered Accountants [[www.icanz.co.nz](http://www.icanz.co.nz)]
- NZ Bankers' Association [[www.nzba.org.nz](http://www.nzba.org.nz)]
- NZ Business Roundtable [[www.nzbr.org.nz](http://www.nzbr.org.nz)]
- NZ Institute of Economic Research [[www.nzier.org.nz](http://www.nzier.org.nz)]
- NZ Exchange [[www.nzx.com](http://www.nzx.com)]

### *Australian government sites*

- Banking Ombudsman [[www.abio.org.au](http://www.abio.org.au)]
- National Office for the Information Economy [[www.ogo.gov.au](http://www.ogo.gov.au)]

### *Australian commercial sites*

- Australian Financial Markets Association [[www.afma.com.au](http://www.afma.com.au)]
- Australian Securities and Investment Commission [[www.asic.gov.au](http://www.asic.gov.au)]
- Australian Stock Exchange [[www.asx.com.au](http://www.asx.com.au)]

### *International sites*

- Bank for International Settlements [[www.bis.org](http://www.bis.org)]
- Global Banking Law Database [[www.gbld.org](http://www.gbld.org)]
- International Monetary Fund [[www.imf.org](http://www.imf.org)]
- International Swaps and Derivatives Association [[www.isda.org](http://www.isda.org)]
- NASDAQ [[www.nasdaq.com](http://www.nasdaq.com)]
- New York Stock Exchange [[www.nyse.com](http://www.nyse.com)]
- United States Securities and Exchange Commission [[www.sec.gov](http://www.sec.gov)]
- World Bank [[www.worldbank.org](http://www.worldbank.org)]