Scope of powers of interim liquidators considered by the High Court of New Zealand: re CBL Insurance Ltd. (in interim liquidation) [2018] NZHC 2547

In one of the decisions arising out of the collapse of New Zealand-based CBL Insurance group ("CBLI"), the High Court of New Zealand was asked to consider whether the powers of interim (provisional) liquidators extended to allowing the interim liquidators to enter into a commutation agreement with CBL Insurance's largest creditor; Elite Insurance, which was a ceding insurer registered in Gibraltar.[1] The effect of the transaction would have been to extinguish CBLI's liabilities to Elite in return for a mixture of cash and non-cash assets. It had been assessed by actuaries as being in the best interests of CBLI's remaining creditors.

In *Re CBL Insurance Ltd (in interim liquidation)*[2] the interim liquidators applied to the High Court for directions that they had the power to enter into the commutation transaction. The application was opposed by the directors of CBLI, the administrators of CBLI's shareholder[3] and another ceding insurer, Alpha Insurance A/S (in liquidation). The opponents challenged both the interim liquidators' power to enter into the transaction, and the expert opinion that it would benefit all creditors.

The Court held that the specific transaction in contemplation was outside of the powers of an interim liquidator, whose role was to maintain the value of assets. Interim liquidators could only exercise their powers to that end. The transaction in question would have had the effect of crystallising and eliminating CBLI's net liability to one of its creditors in circumstances involving the divestment of some of CBLI's assets.

This article considers whether the Court was right to take the approach that it did to the application.

Jurisdiction

Section 246 of the Companies Act 1993 (NZ) empowers the Court to appoint an interim liquidator if satisfied that it is necessary or expedient to maintain the value of the company's assets. The consequent rights and powers (unless limited by the Court) are those of a liquidator to the extent necessary or desirable to maintain the value of the company's assets. An interim liquidator thus has the powers necessary to carry out the general functions and duties of a liquidator under the Act as well as those specifically conferred under the Act, including in Schedule 6.

The Court agreed that the 1993 change in the wording of the section signalled potentially more flexible powers than under the equivalent provisions of the 1955 Companies Act, which replicated the 1948 English Companies Act. Nevertheless, cases decided under s 246 have continued to treat the purpose and powers of an interim liquidator in a very

[1] Elite was placed into run-off in July 2017 by its regulator and required the assets urgently to restore regulatory solvency to avoid liquidation, pursuant to the Solvency II EU Directive for insurance companies that came into force on 1 January 2016.
[2] CBLI was placed into liquidation on 12 November 2018.
[3] The opposition by the first two parties was tactical, as both then adopted the terms of the proposed commutation as an essential component of their joint restructuring proposal.

similar way to that in which the powers conferred under the previous Act were treated. The Court inferred that the change in the wording did not give rise to interim liquidators having broader powers than previously. The Court also acknowledged that the duty to preserve was not absolute in terms, such that there were circumstances in which disposal of assets by an interim liquidator was permissible, albeit rare.

The Court was invited to adopt the approach taken in several recent English and Hong Kong decisions[4] that "*the power to appoint is stated in general terms and the modern tendency is not to restrict or confine its possible application*".[5] This was rejected on the basis that the equivalent English provision[6], states that "*[t]he provisional liquidator shall carry out such functions as the Court may confer on him*", which provides a *very different legislative basis*.

The question then is whether, in the context in which both interim and provisional liquidators may be appointed, the requirements under s 246 create a material limitation on interim liquidators' powers. The distinction drawn by the Court between the position in New Zealand and elsewhere in the Commonwealth may be more apparent than real, notwithstanding the differences in the legislative wording.

In both England and New Zealand, the power to appoint arises upon the presentation of a winding-up petition (Eng)/liquidation application (NZ). In both jurisdictions, the appointment is made at a time and in circumstances in which the outcome of the substantive petition/application is unknown[7]; control of the company may return to directors, or permanent liquidators may be appointed. It has been said that the provisional liquidator must carry out his or her role "*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*".[8]

The English *"paradigm case is one where it appears that the assets of the company may be in jeopardy and urgent steps must be taken to secure the company's assets*."[9]. That mirrors the NZ legislative wording. The termination of the appointment is by Court order, whether upon the winding-up of the company or upon the application of a party to the proceeding.[10] The Court retains a power in both jurisdictions to limit the powers of the appointees. The powers of a liquidator in s 260 and Schedule 6 of the Companies Act (NZ) are broad in scope, including, as the Court noted, the power to compromise creditors' claims.[11]

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[4] *Smith v UIC Insurance Co Ltd* [2001] BCC 11 (QB), *Daewoo Motor Co Ltd v Stormglaze UK Ltd* [2005] EWHC 2799 (Ch), *Re Arm Asset Backed Securities SA* [2013] EWHC 3351 (Ch), [2014] BCC 252 and *Re China Solar Energy Holdings Ltd* [2018] HKCFI 555
[5] Edward Bailey and Hugo Groves: *Corporate Insolvency: Law and Practice* (2017, LexisNexis), citing *Re Namco Ltd* [2003] EWHC 989 (Ch), [2003] 2 BCLC 78; *MHMH Ltd v Carwood Baxter Holdings Ltd* [2004] EWHC 3174 (Ch), [2005] BCC 536.
[6] s 135(4) Insolvency Act 1986.
[7] *HMRC v Rochdale Drinks Distributors Ltd* [2011] EWCA Civ 1116, at [109], per Lewison LJ.
[8] *Re Dry Docks Corp* (1888) 39 Ch D 306 at 312, cited in *Orion International Limited (in liq) v Horne & Anor* NZHC 2458 (3 November 2009), at [15].
[9] *Re ARM Asset Backed Securities SA,* at [40], per David Richards J.
[10] See, for example, *Re Kingscroft Insurance Co Limited* [1994] BCC 343
[11] (a) Although the Court in this case noted at [53] that: "*the compromise of one creditor's claim other than by agreement of the body of creditors or by a liquidator must surely be the exception.*"
(b) An office holder's ability effectively to compromise foreign law claims will depend on the applicability of the *Gibbs rule* and its equivalents in other jurisdictions: see *Bakhshiyeva v Sberbank of Russia & Ors* [2018] EWCA Civ 2802 (18 December 2018); *Mount Albert Borough Council v Australasian Temperance and General Mutual Life Assurance Society* [1938] AC 224 (PC); *Investec Trust*

Furthermore, the use of provisional liquidation as a precursor to a restructuring allows the preservation of assets that could otherwise be in jeopardy, while a restructuring is attempted.[12] This is particularly so when a scheme of arrangement is to be used. This is because there would otherwise be no moratorium in place while a scheme is being promulgated.

The proposed agreement

Against this background, it was argued that an agreement that involves a disposal of substantial assets could be entered into by an interim liquidator because it would preserve the remaining assets for the benefit of other creditors.

One of the premises for the commutation agreement was that the liabilities ceded by Elite to CBLI were among the poorest quality and therefore at the highest risk of crystallising in due course. The expert actuaries had valued the liabilities in a range of between NZD1 billion and NZD1.2 billion. Of those approximately 65% were ceded by Elite. A worst-case scenario could therefore have resulted in a materially lower dividend for all creditors on a liquidation.[13] Thus, paying Elite in exchange for removing all Elite liabilities from the CBLI balance sheet would benefit both Elite (through restoration of regulatory solvency) and CBLI's creditors (through crystallising the amount payable to Elite in relation to volatile liabilities and thus preserving the balance of assets for distribution to the remaining creditor pool). In short, CBLI's net asset position would have improved had the agreement completed.

In *Re Union Accident Insurance Co Ltd* a reduction of the company's liabilities was held to be correlative of the protection of its assets.[14] The Court distinguished this on the basis that it involved closure of a business to reduce expenses, and therefore creditors were not affected. This is an artificial distinction, given that the expert evidence in *CBLI* was that the creditors were better off if the commutation proceeded, as were the creditors in *Union Accident Insurance*, through the reduction in liabilities.

Conclusion

The role of an interim or provisional liquidator is to assume control of a company's assets for the period between the filing of a liquidation application/winding-up petition until that substantive proceeding is resolved. The English legislation and caselaw have allowed for a broader range of purposes for appointment than the "*paradigm case*" referred to by David Richards J. The use of provisional liquidation in most such cases has nevertheless been to preserve assets while the future of the company is determined, be that liquidation or restructuring. While the New Zealand legislation focusses on maintaining the value of a

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(Guernsey) Ltd & Anor v Glenalla Properties Ltd & Ors [2018] UKPC 7 (23 April 2018) [2018] 2 WLR 1465, [2018] WLR(D) 264; *Hong Kong Institute of Education v Aoki Corp* [2004] 2 HKLRD 760.
(c) Given the distinction drawn between the instant case and *China Solar Energy Holdings*, one option open to the court would have been to amend the order of appointment specifically to allow such a transaction.

[12] *Re China Solar Energy Holdings Ltd*, at [27]

[13] This risk was exemplified by Elite reporting to CBLI a reserve strengthening in relation to existing claims on a single line of business from NZD10 million to NZD27 million in the period between the filing and hearing of the application. The IBNR provided for by CBLI management had been NZD4000.

[14] [1972] 1 All ER 1105 (Ch) at 1112

company's assets, this should not constrain interim liquidators to the extent that the Court in *CBLI* decided, when one has regard to dicta from both countries on the role.

Having regard to the particular transaction, it was one that was within the power of an interim liquidator and, based on the uncontested expert actuarial evidence[15], was a transaction that was consistent with an interim liquidator's role of doing least harm to all concerned, while improving the net asset position of the company, albeit by disposing of some assets. In this author's view, a less restrictive approach to the application was therefore open to the Court. [16]

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[15] CBLI's shareholder filed evidence from an insolvency practitioner, but no opponents filed actuarial evidence.
[16] Author's note: the author represented the regulator on this application and on the application by it to liquidate CBLI.