IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

27/8

M. 2121/89

1643

UNDER THE LIFE INSURANCE ACT 1908

IN THE MATTER of ACL INSURANCE LIMITED

BETWEEN THE HONOURABLE WILLIAM PATRICK JEFFRIES

Applicant

AND ACL INSURANCE LIMITED

Respondent

HIGH PRIORITY

Hearing: 2 August 1990

Counsel: D.W. Colbert for plaintiff and the Public Trustee
L. McEntegart for Judicial Managers of ACL Insurance Limited
G.S. Finnigan for I.F.C. Securities Limited (In receivership)
P.J. Wright for Bank of New Zealand
M.R. Dean for Messrs Thorpe, Pittar and Bagnall

Judgment: 14 August 1990

JUDGMENT OF BARKER J

On 21 December 1989, I made an order under S.40A(1) of the Life Insurance Act 1908 ('the LI Act') upon an application made by the Minister of Justice ('the Minister') under S.40A(4). The order appointed two chartered accountants, Messrs Russell Stuart Hay and Rodney Gane Pardington ('the managers') as judicial managers of ACL Insurance Limited ('ACLI'). Before making the order I was satisfied, as

required by S.40A(2) that there was a likelihood that ACLI was or would be unable to meet its liabilities to its policyholders.

Upon their appointment, the managers took control of ACLI, exercising the functions conferred on them by S.40F of the LI Act. They have prepared a full report for this Court as required by S.40H and have served a summary of their report on the persons required to be so served under S.40H(2), including every policyholder.

On 28 June 1990, I made certain orders regarding access to the full report by various parties who seemed to have a special interest. I gave directions under S.40N(2) fixing the parties to be served with the manager's application for directions.

Essential information found in the report can be summarised as follows. ACLI is a wholly owned subsidiary of ACL Corporation Limited ('ACLC') a private company controlled by Messrs J. Pittar, J.A. Bagnall and G.C. Thorpe. ACLI was the main operating company in the group undertaking a range of insurance business. Under the category of 'life insurance', were 2,000 mortgage repayment insurance policies, 4195 annuities, 40 term insurance policies, 3729 bonds, 218 guaranteed income bonds and 302 loan repayment policies. The estimated claims and obligations under the life insurance category amount to $10,484,000 from which may be deducted the

statutory deposit with the Public Trustee of $500,000 made under S.3 of the LI Act.

Under the 'general insurance' category were 1430 life care contracts, 55 fire and general contracts and 500 travel insurance contracts with an estimated total obligation of $1.985 million less the deposit, again $500,000, held by the Public Trustee in terms of the Insurance Companies Deposits Act 1953 (the 'ICD Act').

It soon became clear to the managers that the financial position of ACLI could not support its continued trading nor could it permit the transfer of its insurance obligations and assets to another insurer. Accordingly, the managers promptly advised all policyholders to effect alternative insurance.

The total realisable value of ACLI's assets could be $6.5 million which is the mid-point in a range of estimated realisations; the final outcome is dependent on a number of contingencies and subjective factors. One of the main investments of ACLI is in a retirement village, known as 'Remuera Gardens' Trust'. The rights of ACLI relative to this investment are limited to the receipt of surplus cash flow from the village operations or to any funds that may be realised from the sale of units, subject to the rights of residents secured by way of first mortgage.

The above brief outline of ACLI's position probably will

change when the assets are ultimately realised. Suffice it to say that ACLI is hopelessly insolvent with no possibility of rehabilitation and with no prospect of paying anything to its numerous unsecured creditors; the order appointing the judicial managers has been shown to have been amply justified.

ACLI had given two series of registered debentures. The first was to IFC Securities Limited (In Receivership) ('IFC') to which ACL gave a debenture dated 12 November 1987 which secured the obligations of ACL to IFC under a loan agreement of even date. Default occurred under the loan agreement. Clause 5 of the debenture created a fixed charge as regards ACLI's freehold and leasehold land, fixed assets, patents, tradenames, trademarks, licenses, shares and capital of any company or corporation unpaid and uncalled capital, goodwill and book debts plus a floating charge over the balance of the assets.

The standard form debenture also provided for automatic crystallisation of the floating charge upon certain events, including default in any of its terms; on the occurrence of default, the debenture holder, at its option, could exercise the powers under the debenture provided, where the default was non-payment of money, written notice had to be given and 7 days required for remedying. ACLI defaulted in meeting a monthly interest payment due on 5 June 1989 and 7 days' notice of default was given. The default which was not remedied in time,

occurred before the appointment of the managers. For this reason, it is said that the 'floating' charge crystallised prior to the date of appointment of the managers. There is litigation pending between IFC and ACLI concerning the validity of the debentures and of various other documentation; it is not relevant to discuss this litigation for present purposes.

Another debenture in favour of the Bank of New Zealand ('BNZ') in standard form dated 28 March 1988, covered all real and personal property of ACLI; again, there was the same differentiation as in IFC's debenture between the property and assets over which BNZ had fixed and floating charges. This debenture, although registered after the IFC debenture, was granted priority for up to $500,000. The amount said to be owing by ACLI under the IFC debenture is over $3.5 million. Messrs Thorpe, Bagnall and Pittar, represented separately by Miss Dean, are directors and shareholders of ACLI. They were guarantors under the debentures, although there is some argument over their liability under the IFC debenture. However, they clearly had an interest in approving the managers' present application.

There was agreement amongst counsel that, regardless of the litigation about the validity of the debenture, there were simply insufficient assets in ACLI to pay the secured creditors as well as the present and likely future costs of the managers. Hence, the managers' application for

directions to be paid in priority to all creditors, including the secured creditors.

The principal question for determination by the Court is whether the fees and expenses of the judicial managers take priority over the claims of the debenture holders. There are also questions relating to the deposits held by the Public Trustee which I shall address later in this judgment.

The managers were supported in their claim that their costs take priority over the secured creditors by the Minister and the Public Trustee. Opposing the argument were the debenture holders and the shareholders and the directors of ACLI who were also guarantors of the debentures.

This is the first occasion on which Part IA of the LI Act has been considered by the Court since that Part was enacted in 1985. The Minister is empowered to apply to the Court for the appointment of judicial managers of a life insurance company "where it appears that there is a likelihood that the company is or will be unable to meet any of its liabilities to policy holders" (See S.40A(2). In determining whether there is such a likelihood, the Court may have (and in this case did have) regard to reports from the Government Actuary and an investigating chartered accountant (Mr J.A. Waller). Once a manager has been appointed, there is a moratorium imposed on

proceedings against the company as set out in S.40B and a prohibition against removal of its assets under S.40C. The management of the company vests in the manager under S.40D.

Under S.40F, the manager is required to carry on the business of a company "in order to preserve and keep intact so far as practicable the property and assets of the company". The manager may exercise all the powers of the company in respect of which he is appointed as is necessary to carry out the functions under the Act; the manager may not, without the approval of the Court, given in respect of any policy or class of policies, issue or grant policies of insurance. The manager may transfer the company's business with the approval of the Court. He may apply to wind up the company (a step which has been recommended here). Reference to Part IA will reveal further detail of the managers' powers and responsibilities.

The starting point in the present application is S.40P relating to the expenses of judicial management; it provides -

> "All costs charges and expenses properly incurred by a judicial manager in the exercise of his functions and powers under this Act (including such remuneration as may be approved by the Court) shall be payable out of the property of the company in respect of which the judicial manager is appointed in priority to all other claims."

One of the managers, Mr Pardington, has filed an affidavit detailing the extensive costs and expenses incurred by the managers to date. There is no challenge to the quantum of the managers' remuneration which is calculated on the scale normally charged by their firm for principals and others. There is debate over the quantum of the fees incurred by the managers for legal advice and also whether the charges for legal expenses incurred in litigation with IFC were properly incurred. These arguments do not need to be resolved in this judgment.

The scenario provided by Part IA of the LI Act is a variation on a fairly regular theme which has seen statutory managers imposed on a whole range of companies in the public interest. In recent troubled financial times, there has been frequent exercise of the powers of the Executive under the Companies (Special Investigations) Act 1958 ('the 1958 Act'), and its succcessor, the Corporations (Investigation and Management) Act 1989 ('the 1989 Act'). The Reserve Bank of New Zealand Amendment Act 1989 ('the Reserve Bank Act') gives similar powers to the Reserve Bank in respect of registered banks. Virtually each statutory management ordered thus far has resulted in complex litigation. However, none of the other cognate statutes reposes the power of appointment of managers in this Court. Nor are any of the other kinds of manager called 'judicial manager' with a duty to report to the Court.

Clearly the provisions presently under consideration must be interpreted in the context of the LI Act. S.40P is unambiguous on its face, and expressly provides for the payment of judicial managers "in priority to all other claims". Counsel for the debenture-holders submitted that in terms of S.40P, such payment may only be made "out of the property of the company" and further submitted that property subject to a fixed charge or a crystallised floating charge did not fall within the term "property of the company".

There is some support for this view in those cases interpreting S.299 of the Companies Act 1955 which is of similar thrust to S.40P. S.299 provides -

> "All costs, charges and expenses properly incurred in the winding-up, including the remuneration of the liquidator shall be payable out of the assets of the company in priority to all other claims."

In McDonald & Anor v Australian Guarantee Corporation (NZ) Ltd & Ors, (1990) 1 NZLR 227 Wallace J found that the word 'assets' in S.299 and its English equivalent has been interpreted in a long series of cases to mean 'free assets'. For example, Re Willis C. Raymond Limited (In Liquidation) [1928] NZLR 115. Subsequently, it has been held that the word 'assets' includes both the free assets of the company and assets subject to a floating charge. See Re Barleycorn Enterprises Limited [1970] Ch 465 and Re Pacific Print Finishers Limited (1987) 3 NZCLC 99,856.

Wallace J noted that the word 'assets' did not extend to assets subject to a fixed charge or to a floating charge which had crystallised before the date of liquidation. See Re Christonette International Ltd [1982] 3 All ER 225.

Wallace J then considered, without deciding, an argument that in S.65 of the 1989 Act the word 'property' had been deliberately used to avoid the historical interpretation of the word 'assets'. For this reason, it was argued, cases concerning ordinary liquidations should not be transferred into the different regime established under the 1989 Act. Wallace J said of this argument at 247 -

> "While those responsible for the drafting of the Investigation and Management Act would no doubt have been well aware of the decisions concerning S.299 of the Companies Act, I am reluctant to hold that decisions which possibly reflect an earlier view and a different situation pertaining to a liquidation should govern the interpretation of the Investigation and Management Act which itself was introduced to provide a new regime to deal with the situation where the old law was inadequate. I do not, therefore, for the purpose of this judgment place weight on the decisions concerning the interpretation of S.299."

Counsel in the present case referred also to the decision of Ellis J in Cowan v Rowe (1990) 5 NZCLC 66,215. That was a case concerning the 1958 Act where statutory managers had sold land belonging to a company in statutory management. After paying disbursements of sale, they held a small sum which they claimed towards the costs of receivership; the debenture holders claimed it belonged to them pursuant to the fixed charge.

Ellis J held that the expression 'assets of the company' in S.11 of the 1958 Act referred to its free assets after satisfaction of fixed charges. He considered that the scheme of the Act referred to the interest of secured and unsecured creditors and it did not give statutory receivers the power to have their charges paid in priority to secured creditors. The learned Judge held that S.11 of the 1958 Act had been enacted on the basis of the long established gloss that 'assets' meant 'net assets'. The learned Judge followed McDonald's case, referring to many of the authorities cited in Wallace J's judgment.

Like Wallace J, however, I am unable to place much reliance on cases decided under S.299 of the Companies act 1955. As in McDonald's case, S.40P uses the word 'property', not 'assets' and it may well be that this word was deliberately chosen to avoid the interpretation historically given to the word 'assets'.

I note also that elsewhere in Part IA of the LI Act, that property subject to security is consistently referred to as the property of the company in management.

Thus S.40B(2)(d) prohibits action taken under a "debenture, ... or other security over the property of [the] company..." once the company is subject to judicial management. Similarly, S.40B(5) provides that S.40B(2) shall not affect the existence or priority if "any security over the property of [the] company..." These

phrases clearly indicated that such property is still considered "property of the company", notwithstanding that there may be a security over it.

I can see no justification for a different interpretation of the words "property of the company" in S.40P. I am therefore of the view that S.40P means exactly what it says, and provides for the payment of judicial managers in priority to all other claims.

Although Wallace J in McDonald's case held that S.65 of the 1989 Act, equivalent to S.40P, does not confer a right on statutory managers to recover their costs in priority to the claims of secured creditors, the learned Judge was there concerned to interpret two apparently conflicting sections. That part of his judgment is headed "The second issue: the interrelationship of S.65 and S.51(2)" at p.245 et seq.

The learned Judge held that S.51(2) of the 1989 Act prevailed over S.65 of the same act. S.51(2) provides for payment to a chargeholder, upon the sale of property, the subject of his charge, in priority to all other claims other than the cost of the statutory manager in selling the property and claims under S.308 of the Companies Act.

There is no equivalent to S.51(2) of the 1989 Act in part IA of the LI Act, however. Counsel for BNZ sought to place reliance on S.40B(5) which provides -

> "Subject to the provisions of this Act nothing in subsection (2) of this section shall affect the existence of any security over the property of any company to which this section applies or its priority in relation to other debts."

However, I do not consider that subsection by any means the equivalent of S.51(2) of the 1989 Act. First, S.40B(5) is expressed to be "subject to the provisions of this Act" which of course includes S.40P. Secondly, nothing in S.40B(5) purports to give priority to the debenture-holders: - on the contrary, all the subsection provides is that nothing in subsection (2) shall affect existing priorities. Subsection (2) does not relate to priorities at all, but prohibits certain actions without the leave of the Court, once judicial managers are appointed.

I am therefore satisfied that, unlike McDonald's case, there is nothing in the LI Act to displace the ordinary meaning to be attached to the wording of S.40P.

I note also that Wallace J referred in McDonald's case to the clear policy decision in S.51(2) of the 1989 Act that only the costs of the statutory manager in selling or disposing of property or assets of the company were to be paid in priority to the claims of the secured charge holders. There is no comparable statement of policy in Part IA of the LI Act.

I am able to take a different view about the procedures

under the LI Act. They are unique in that the responsibility for appointing managers rests not on the Executive (as it does under the 1989 Act) but on this Court. It follows that the judicial managers are officers of the Court. Their situation is more akin to Court-appointed receivers than to statutory managers.

There is a line of authority which indicates that Court-appointed receivers should be paid their remuneration and expenses in priority to secured creditors. The rationale is that, if the debenture holder had appointed the receiver or manager himself and not asked the Court to appoint him, then he would be bound to pay him for attending to the company's affairs. In Batten v Wedgewood Coal & Iron Co Ltd (1884) 28 Ch.D.317, 324 Pearson J said in a case concerning a Court-appointed receiver -

> "Ought the receiver to be paid before it can be said there is anything to distribute in payment of costs or anything else? In my opinion, that is a receiver's position. He is the officer of the Court, and the Court is bound to see he is paid just as if the trustees employed a manager they would have been bound to pay him without regard to the sufficiency of the estate to meet the claims upon it. I think the Court is bound to see the receiver is paid."

Likewise in Re Beni-Felkai Mining Company Ltd, [1934] 1 Ch 406, 419 Maugham J (as he then was) said -

> "..a debenture holder's receiver, in a case where the receiver has been appointed by the Court, is in a different position to that of a

> liquidator. Such a receiver is the officer of the Court, and I can see no reason for coming to the conclusion that the liquidator in a voluntary winding up, whose remuneration has been fixed by shareholders who may have no interest in the ultimate assets, is in the same position as an officer of the Court. The latter has his remuneration provided for in front, as far as possible, of every other payment to be made out the assets of which the Court has assumed control."

Court-appointed receivers under a debenture are rare in this country, as is noted in the New Zealand commentary to Halsbury (4th ed) vol 39 on Receivers. The Court can appoint receivers under its equitable jurisdiction and has done so from time to time. For example, Re Samco-Sargent Consolidated Limited & Ors (M.832/77, Auckland Registry, judgment 8 July 1977).

Because the judicial managers are officers of the Court, appointed by the Court, I consider that the line of authority more appropriate to their position is that relating to Court-appointed receivers rather than that relating to liquidators or statutory managers. Moreover, the absence of a provision equivalent to S.51(2) of the 1989 Act assists my conclusion. I note too that the emphasis in Part IA of the LI Act is to preserve the assets of the company rather than to liquidate them.

Accordingly, I rule that the remuneration and expenses of the managers are to be paid in priority to the claims of all creditors, including secured creditors.

The next direction sought is concerned with the two funds of $500,000 held by the Public Trustee. Counsel accepted that these funds are held in trust for policyholders (one for 'life' policy holders and one for 'general' policy holders).

A problem has arisen regarding the cost of assessing claims of which there are many. Should these expenses come out of the funds or should they be paid by the managers out of ACLI's other meagre assets, at the expense of the secured creditors.

Each fund is governed by a different Act. The $500,000 deposit for life insurance is held by the Public Trustee under the LI Act and the $500,000 deposit for general insurance under the ICD Act. There are similar provisions in each Act, although the ICD appears the more comprehensive.

The managers are reluctant to have the claims under the policies assessed - presumably by loss adjusters - until they know where the cost of assessment is coming from and how much will be available for claimants. A large sum has been mentioned as the cost of processing the claims.

I am reluctant to give directions in this area without the benefit of argument on behalf of the policy holders/claimants. I therefore await the nomination of counsel of reasonable seniority, prepared to accept

appointment on behalf of all policyholders in ACLI and to sign the usual undertaking. Since each fund is separate and there can be no overflow from one into the other, I see no difficulty in one counsel representing both sets of policyholders. The order of appointment can be made by any Judge. I shall hear further argument on 8 November 1990. The motion for further directions is adjourned to that date.

Prior to that resumed hearing, the managers must supply greater detail as to the numbers of claims (as distinct from policies) in each category and likely quantum of claims as well as accurate estimates of the costs of assessing claims. Counsel appointed for the policyholders may also require additional information from them. Some claims, I imagine, can be accepted with little difficulty - e.g. proof of death of a life assured. Others - even for smaller amounts - might require greater scrutiny - e.g. travel insurance claims. Based on the information supplied, the argument should be a legal one, although all parties are at liberty to file further affidavits. Counsel may ponder whether it is just that these policyholders with easily assessed-claims should contribute to the cost of assessing difficult claims.

I also note for the assistance of counsel at the later hearing, the following points which are either self evident from the statute or settled law -

(a) The managers (on behalf of ACLI) are entitled to the income from the deposits (S.5 of the LI Act; S.14 ICD Act). There may be an argument whether the Public Trustee has the right to deduct administration charges/commission before paying the income over to the managers (S.13A of LI Act and S.24 of ICD Act relate to the Public Trustee's remuneration).

(b) The deposits are held on trust for policy holders (S.8 LI Act; S.12 ICD Act).

(c) There are provisions relating to the application of securities held by the Public Trustee which apply on the liquidation of the insurance company (S.8A of the LI Act; SS.12A-D of the ICD Act). The question therefore arises whether ACLI should be placed in liquidation. The managers have recommended it - a recommendation expressly contemplated by S.40F(b)(iii) and there seems no contrary indication. I direct that any winding-up application which the managers may decide to bring be heard on 8 November also. The time between now and that date should be sufficient for the formalities of winding-up to occur. Once ACLI has been wound up, then the sections just referred to will come into play. Nothing in the LI Act appears to stop the managers continuing in office after a winding-up order has been made.

(d) There is authority for the Court to order that the expenses of distributing trust moneys are to come out of those moneys in situations such as ACLI's where there are just no other funds to pay the expenses. See Re Landbase Securities Ltd (In Liquidation) (1989), 4 NZCLC 65,093 and Re Secureland Mortgage Investments Ltd (No 2) (1988) 4 NZCLC 64,266.

There will be a direction that the costs and expenses of the managers as approved by the Court be paid out of the assets of ACLI (excluding the statutory funds held by the Public Trustee) in priority to all other claims including the claims of secured creditors. The directions hearing is adjourned to 8 November 1990.

I await a memorandum from counsel concerning the managers' costs and expenses to date. Costs of the present hearing reserved, to be argued on 8 November 1990.

R. D. Barker J.

Solicitors: Crown Solicitor, Auckland, for plaintiff and Public Trustee
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Phillips Nicholson, Auckland, for IFC
Buddle Findlay, Auckland, for BNZ
Russell McVeagh McKenzie Bartleet & Co, Auckland, for Messrs Thorpe, Pittar & Bagnall

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