IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2012-404-002217
[2012] NZHC 1396

IN THE MATTER OF	a scheme of arrangement under Part 15 of the Companies Act 1993
BETWEEN	ACS (NZ) LIMITED Applicant

Hearing: 19 June 2012

Appearances: M D Arthur and J A McMillan for Applicant
S Barker for Reserve Bank
S Hunter for Roman Catholic Bishop
R Lange for Arts Centre, Christchurch
M Corlett for Ansvar Clients Committee
J Ormsby and J Day for Church Property Trustees of the Anglican Diocese of Christchurch
S Neville for Thornton Tomasetti

Judgment: 19 June 2012

ORAL JUDGMENT OF VENNING J

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[1] ACS (NZ) Limited (ACS) seeks orders approving a scheme of arrangement under Part 15 of the Companies Act 1993. The scheme of arrangement is intended to effect the managed withdrawal by ACS from its insurance business in New Zealand. ACS has cancelled the policies it underwrote and is not issuing new policies. Its present business is limited to managing the remaining and outstanding claims under policies it formerly wrote.

[2] In broad terms the proposed scheme provides for business to carry on as normal during an initial scheme period. During that period claims will be paid in the ordinary course, the directors will remain in the control of the company and the scheme administrators will play a monitoring role. A trigger event will occur if at any time it appears that, without the operation of the scheme, there would be no reasonable prospect that ACS could avoid going into liquidation. That would trigger the reserving period. During that period the scheme administrators will control the company. In that period the company will pay claims on a pro rata basis having regard to charges otherwise enforceable under s 9 of the Law Reform Act 1936. Scheme creditors will not be able to enforce against the company during the reserving period. The scheme creditors are those creditors with claims arising out of the insurance contracts previously written.

[3] The application is made under Part 15 of the Companies Act 1993 in particular s 236. The application of s 236 and its predecessors has been considered by the Court of Appeal on a number of occasions. I refer to the decision of *Weatherston v Waltus Property Investments Limited.*[1] The Court noted that the scope and power of the Court under s 236 is to be considered in light of the legislative intention the Court should have a broad discretion, limited only by the policy and purposes of the Companies Act.

[4] In the *Weatherston* decision the Court referred with approval to the following principles set out Smith J in *Re C M Banks Ltd:*[2]

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1 *Weatherston v Waltus Property Investments Limited* [2001] 2 NZLR 203 (CA)

2 *Re C M Banks Ltd* [1944] NZLR 248 at 253.

> The duty of the Court is to see (1) that there has been compliance with the statutory provisions as to meetings, resolutions, the application to the Court, and the like; (2) that the scheme has been fairly put before the class or classes concerned; and that if a circular or circulars have been sent out, as is usual, whether before or after the making of the application to the Court, they give all the information reasonably necessary to enable the recipients to judge and vote upon the proposals; (3) that the class was fairly represented by those who attended the meeting and that the statutory majority are acting *bona fide* and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent; and (4) that the scheme is such that an intelligent and honest man of business, a member of the class concerned and acting in respect of his interest, might reasonably approve.

[5] Though there may have been some suggestion in the case of *Suspended Ceilings (Wellington) Ltd v Commissioner of Inland Revenue*[3] that a more stringent, reasonableness test rather than the intelligent and honest person of business might be applicable, in *Weatherston* the Court of Appeal suggested that the *Suspended Ceilings'* test may not be pertinent beyond its particular context.

[6] I also note that in *Weatherston* the Court referred to Canadian authority with approval where the Court had supplemented the test of an intelligent and honest business person by consideration of whether the arrangement was generally fair and equitable. The Court observed that the combination of both tests is clearly apt in the context of the Act where competing interests, which must be balanced by the Court in deciding whether and, if so, on what basis to approve, in that case an amalgamation proposal. The combination of considerations is equally applicable to the scheme of arrangement before this Court.

[7] The applicant has promoted the scheme of arrangement in this case because it considered that it will provide a smoother transition from solvency to potential insolvency in the event that occurs for ACS in the course of managing the run-off of its existing obligations.

[8] It is submitted on behalf of ACS that with the additional support the scheme proposes from its parent Ecclesiastical Insurance Office there should be sufficient assets and reinsurance to enable it to pay all claims of scheme creditors in full in the

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[3] *Suspended Ceilings (Wellington) Ltd v Commissioner of Inland Revenue* (1997) 8 NZCLC 261,318 (CA).

normal course but it accepts that that may not be the case. The claims to which ACS is exposed as a result of the Canterbury earthquakes leave the position uncertain. ACS faces a number of large claims and it is not possible to determine their ultimate impact in terms of solvency with complete certainty.

[9] For that reason it is submitted that the most responsible course was for ACS to establish a process to deal with the potential future insolvency, even though ACS does not consider it is necessary at this time to appoint liquidators.

[10] The scheme proposed therefore intends to allow the company to continue trading under the control of its directors for the time being but also to agree a formal and structured compromise regime should it be determined at a later date ACS may be insolvent. It is at that stage the scheme administrators would take direct control of ACS and the claims it faces from scheme creditors.

[11] In the course of submissions on behalf of the applicant counsel referred to the application of the schemes of arrangement in other instances in insurance companies, noting for example the case of *Re HIH Casualty and General Insurance (NZ) Ltd (in liquidation).*[4]

[12] ACS holds substantial reinsurance. ACS has accepted, in the course of discussion with the interested scheme creditors, the findings in *Re Western Pacific Insurance Ltd (in liq); Ruscoe v Canterbury Policy Holders*[5] to the effect that s 9 applies to reinsurance and that ACS' liability to scheme creditors was a charge on the reinsurance money payable to ACS under its reinsurance. I will refer to that later.

[13] On 1 May, on an ex parte application which ACS served on a number of interested parties including the Reserve Bank, the Court made a number of orders designed to comply with s 236(2). The Court made directions:

- that the application be brought to the attention of affected persons;

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4 *Re HIH Casualty and General Insurance (NZ) Ltd (in liquidation)* HC Auckland CIV-2009-404-3637, 10 September 2010.

5 *Re Western Pacific Insurance Ltd (in liq); Ruscoe v Canterbury Policy Holders* (2011) 9 NZBLC 103,483.

- that there be a meeting of those persons,

- determining the persons that constitute a class of creditors, confirming in this case, that a single class of creditors was applicable;

- providing for notice of the meeting;

- providing for the reporting of the results of the meeting; and

- to apply in the event that any of the affected parties opposed the scheme and the application for approval.

[14] The order made on 1 May also provided in detail for the provision of further information to affected parties.

[15] At an earlier stage an issue was raised whether it was appropriate that scheme creditors vote as a single class but that matter has not been advanced today. No formal opposition has been raised about that issue.

[16] If necessary I would be content to accept that, in light of the discussion of the issue in the cases of *Re Hawk Insurance Co Ltd,*[6] *Sovereign Life Assurance v Dodd*[7] and *Re British Aviation Insurance Co,*[8] when regard is had to the emphasis on rights rather than interests and that the relevant rights are the existing rights of persons to be bound by the scheme as opposed to their rights under the scheme, and that the Court is required to consider the comparison between the rights that would in reality exist in the absence of the scheme, that it was appropriate in this case for the scheme creditors to be regarded as members of a single class for voting purposes.

[17] Following the orders and directions made on 1 May, the further information was provided and notice of the meeting was given in accordance with the directions. There was a slight delay in the provision of some information to affected parties but

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6 *Re Hawk Insurance Co Ltd* [2002] BCC 300.
7 *Sovereign Life Assurance v Dodd* [1892] 2 QB 573.
8 *Re British Aviation Insurance Co* [2006] 1 BCLC 665.

I accept the delay was not substantive and nor should it prevent this Court considering the outcome of the meeting.

[18] Apart from noting the delay of the provision of information no party represented before the Court has taken the position they have been prejudiced.

[19] At the meeting on 12 June the scheme was approved by the requisite majority, both in number and value. The applicant now seeks this Court's approval to the scheme.

[20] A number of parties filed formal notices of opposition or notices of appearance and some are represented before the Court this morning.

[21] The Reserve Bank of New Zealand is represented. I will return to the Bank's position in a moment.

[22] The Church Property Trustees of the Anglican Diocese of Christchurch filed a formal notice of opposition. Mr Ormsby confirmed that the Church Property Trustees' position is that, after receiving the further information provided, and further assurances from the applicant, including undertakings and an agreement to make the amendments proposed by Mr Ormsby's client, his client voted in favour of the scheme and considers it to be in the best interests of the scheme creditors generally.

[23] Mr Lange confirmed that the Arts Centre, which also filed papers, voted in favour of the scheme and abides the decision of the Court.

[24] The Roman Catholic Bishop of the Diocese of Christchurch also filed a formal notice of opposition. Mr Hunter confirmed that at the meeting his client voted in favour of the scheme and abides the decision of the Court. He notes that the amendment sought by his client has been agreed to by the applicant.

[25] The ACS Client Support Group voted in favour of the scheme. Mr Corlett confirms it abides the decision. Rangi Ruru School had voted against the scheme and had filed a notice of opposition. However Mr Corlett advised the Court that the

notice of opposition could be regarded as withdrawn and the school abided the decision of this Court.

[26] Thornton Tomasetti Inc has filed papers but Ms Neville accepts that, given it is in a different position it now does not seek to be heard in opposition to the scheme.

[27] A Mr Mundy, who had filed papers at an earlier stage, also filed papers for the hearing this morning. Mr Mundy considers the scheme was put together with undue haste. He was concerned he had not had sufficient time to consider his position. I acknowledge Mr Mundy's concern as noted in his material. However, parties with I suspect, substantially more resources than Mr Mundy, have been able to consider the matter in rather more detail than he has. I note the voting in favour of the scheme at the meeting which Mr Mundy attended was overwhelmingly in support of the scheme, both in terms of the numbers voting at the meeting and in terms of the value of the scheme creditors' claims.

[28] I return to the position of the Reserve Bank. Mr Barker very fairly outlined the position of the Bank. The Bank has standing to be heard in relation to an application such as this for approval of the scheme.[9]

[29] The Bank did not take any direct action to stop the scheme and considered it appropriate that a vote be held on the scheme. In general terms the Bank respects the will of the creditors and claimants as expressed in the vote. Nevertheless Mr Barker outlined a number of concerns that the Bank holds in relation to the scheme.

[30] First Mr Barker made the point that it was incorrect to say that an overwhelming majority of creditors favoured the scheme. He suggested that only a small minority by number of creditors voted on the scheme and the vast majority by number had not voted. While strictly that is correct, nevertheless, of those creditors or insured who were interested enough to attend the meeting or supply a proxy or postal vote the vast majority supported the scheme. Of the 146 creditors or insured voting 139 voted in favour as against only seven against.

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9 Insurance (Prudential Supervision) Act 2010, s 156(3).

[31] Further the support of creditors by value was even more significant. For the purposes of voting ACS accepted the various insured's assessment of their claims. On that basis in excess of $888 million voted in favour out of a total of $934.6 million, which was approximately 95 per cent in favour. ACS tested that result by having regard to the reserves that it had applied to the same claims. The result was that those voting in favour represented $417.7 million out of a total reserve for claims of $445.8 million, which was approximately 93.7 per cent in favour.

[32] The Bank makes the point that it is of concern there is such a difference between the value of the claims assessed by claimants as opposed to the reserves that ACS has attributed to those claims. However, as noted ACS accepted the value of the claims as proposed by the claimants for the purposes of voting. It is fair to say that one would not expect the claimants to have understated their claims at that stage. No doubt during the claims settlement process the parties will have to revise their particular estimates of claims. Importantly, in my view, the difference between the quantum of the claims voting in favour of the scheme whichever approach is taken is not dissimilar. The percentage supporting the scheme is close to 95 per cent in value.

[33] The Bank is also concerned that, as opposed to the situation in a liquidation, the scheme does not provide for the pari passu principle. On the analysis carried out by KPMG there is a real issue whether ACS would be able to meet the solvency requirements under the Insurance (Prudential Supervision) Act 2010 by 30 June 2012, which is a condition of its provisional licence so that it could, very shortly be placed into liquidation.

[34] The KPMG report suggests there is a 25 per cent chance of ACS failing to meet that solvency test. But it has to be noted that KPMG has accepted that the estimate of solvency is a difficult exercise. KPMG acknowledges that the earthquakes and the claims arising out of the earthquakes present substantial complexity. In the introduction to their report KPMG acknowledges the range of possible final results as wide, and the final outcome may fall above their 90 per cent probability of sufficiency or may fall below the central estimate provided. They go on to say the results of the report should not be interpreted as providing a range of

possible outcomes. The report essentially acknowledges that the matter will need to be considered and reassessed over the coming months as further information emerges.

[35] I note that the KPMG report was made available to scheme creditors before the meeting and that, despite what was set out in the report, the scheme creditors still voted in favour of the scheme. I also note that the chair of the meeting suggested that ACS had its own actuarial reports which supported the view ACS would be able to comply with the more stringent solvency test required by the Insurance (Prudential Supervision) Act.

[36] Mr Arthur also made the point which I accept has some force, that ultimately the directors who remain in control of the company under the scheme until a triggering event occurs will be particularly mindful and aware of their obligations in relation to solvency and in relation to the certificate that they will be required to provide to the Bank in terms of whether ACS is able to meet the solvency requirements of the Insurance (Prudential Supervision) Act.

[37] While, unlike the application of the pari passu principle that applies in a liquidation, the scheme creditors paid before a trigger event may recover more than creditors paid after the event, that is the practical position that would apply in the event of an ultimate liquidation if the scheme was not approved. ACS is not currently insolvent.

[38] While liquidators could claw back previous payments and settlements, as Mr McCloy has noted in his affidavit[10] it would not necessarily follow that a liquidator would seek to claw back any or all payments made by ACS prior to any liquidation. The liquidator would be required to consider a number of factors, including whether the recipient had altered their position in the reliance on the receipt of the proceeds, whether recovery of the voidable transaction claim was economically viable and also the consideration, which is a very real consideration in the settlement of insurance

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[10] Mr McCloy is an experienced receiver and liquidator and it is proposed he be one of the two scheme administrators.

claims, whether the payment represented a good settlement at an amount below the reserve held by ACS for the particular claim.

[39] There is also the further point made by Mr McCloy and addressed in submissions by Mr Arthur that the scheme enables the creditors committee to raise the issue with the scheme administrators or even the company itself as to whether a meeting of scheme creditors should be held to vote on termination of the scheme and the appointment of liquidators.

[40] Mr Barker also noted the Bank's concern at the ability of the percentages paid out to claimants to be reduced during the course of the operation of the scheme. He noted that the scheme was broad enough to enable not only a "top-up" but also a reduction in the percentage paid to claimants. However, I accept Mr McCloy's point in response, which is consistent with the practicality of the situation, that in the event the scheme administrators are required to manage the business it is extremely likely that they will adopt a conservative approach to the assessment of outstanding claims, the reinsurance and other assets of ACS available to meet those claims, together with the likely costs of continuing the scheme and ACS' operation to the extent it is necessary to do so. On the basis of such a conservative assessment and approach it is likely they will pay out less than they anticipate might ultimately be payable to scheme creditors rather than initially paying out the maximum percentage assessed as payable and then later reducing such pay-outs.

[41] The matters raised by Mr Barker on behalf of the Bank are properly raised but I am satisfied that, on the balance, they are answered by the provisions of this particular scheme and the responses that I have referred to.

[42] Further, there are a number of other factors that support the Court's approval of the scheme in this case. As was observed by Mr Ormsby and accepted by other counsel, an important factor is that the scheme provides the best opportunity for an ordered and efficient run-off and management of claims with minimal disruption in relation to the company's processes as opposed to the situation of a liquidation.

[43] It is inevitable that if a liquidation occurred the liquidators would need some time to familiarise themselves with the operation of the company. They would proceed on a cautious basis which would likely result in material delay in meeting claims. There may also be issues with reinsurers and their willingness to co-operate. Further, there may well be additional costs associated with the liquidation which the scheme would avoid. Finally there is the potential for more ready challenges to decisions by the liquidators through the Court process. I accept it is fair to say that a liquidation would almost certainly result in more disruption and uncertainty compared to the scheme, which is a significant factor in terms of the ongoing management of the claims of the various claimants, and that is a significant factor in favour of the scheme.

[44] Further, and quite apart from that, there is the additional support estimated at approximately $22 million which, upon approval of the scheme, Ecclesiastical Insurance Office is to provide. Mr Arthur has drawn the Court's attention to the reserves and the reinsurance position, particularly in relation to the February 2011 earthquake. The availability of a further $22 million in relation to those claims is a significant factor in favour of the approval of the scheme.

[45] Finally I also note that in terms of ongoing protection of the scheme creditors' interests the scheme provides for a well supported creditors committee and that at the meeting on the 12 June, seven independent representatives were chosen for the creditors committee.

[46] Standing back and reviewing the matter overall I am satisfied that the scheme is one that an intelligent and honest person in business might reasonably approve. I am supported in coming to that view by the significant level of support for the scheme at the creditors' meeting.

[47] In summary I am satisfied that the applicant has complied with the relevant statutory provisions as to the meetings and the information provided to the interested parties before the meeting, that the interested claimants were fairly represented by those attending the meeting and that those voting in favour of the scheme were acting bona fide in doing so. As noted, I have already concluded that the scheme is

such that an intelligent person would reasonably approve. Having considered the matters raised by the Bank I am still satisfied that it is a fair and equitable arrangement in the unfortunate circumstances that the claimants and ACS find themselves as a consequence of the earthquakes in Canterbury.

[48] I therefore approve the scheme in its amended form.

[49] I record that the scheme put to the meeting provided for amendments to be made (clause 51) and that the amendments proposed to be made and sanctioned by this Court in the draft presented to the Court today are supported by the claimants represented today. I am satisfied they are proper and appropriate amendments.

[50] I also formally record the undertaking by ACS, Ansvar Insurance Limited and Ecclesiastical Insurance Office not to challenge the *Western Pacific* decision and the further undertaking by ACS that where more than 50 per cent in value of scheme creditors seek a meeting of scheme creditors, a meeting will be convened.

Orders

1 The proposed scheme of arrangement between the applicant (ACS) and its creditors, as described in the amended Scheme of Arrangement presented to the Court, is approved and is binding upon ACS and each of its creditors, as well as Ansvar Insurance Limited, Ecclesiastical Insurance Office Plc, The Trustee (as defined in the Scheme) and the Scheme Administrators in accordance with its terms, with effect from the Effective Date as defined in the Scheme, being 20 June 2012;

2 ACS is granted leave to apply to the Court at short notice for any necessary approval of any amendment, modification or supplement to the Scheme; and

3 If liquidators are appointed to ACS, the Scheme will continue in effect and be binding on the liquidators of ACS unless and until the Court orders otherwise.

Venning J