

## **APPENDIX TWO: REGULATORY IMPACT STATEMENT**

### **Statement of the Nature and Magnitude of the Problem and the Need for Government Action**

A cross-border insolvency arises when an insolvent entity is placed in a form of insolvency administration in one country but has assets or debts in other countries.

Cross-border insolvency proceedings can be inefficient and costly, particularly where the rules that apply to the proceedings in each country are not clear. This arises in part because there is currently no uniformity of approach to the initiation of cross-border insolvency proceedings. In addition, the costs of accessing foreign courts, or bringing separate proceedings in another country, can be prohibitive.

The increase in global trade and cross-border transactions heightens the likelihood of cross-border insolvency proceedings involving New Zealand businesses. While there have been relatively few cases to date of cross-border insolvency proceedings involving New Zealand businesses, those cases that have occurred overseas have been expensive, complex and lengthy. There is no typical case of cross-border insolvency and there are no figures kept. However, the assumption is that situations of cross-border insolvency will usually (but not always) involve substantial sized companies with substantial debts in both countries.

Last year, the government agreed to amend the current rules by adopting the UNCITRAL Model Law on Cross-Border insolvency. The model law goes some way towards addressing the problems identified by establishing a procedure for co-operation between states in the event of a cross-border insolvency. However, it does not address the issues of cost associated with accessing foreign courts or require a single insolvency proceeding for any given person or entity.

The differences between the insolvency regimes in New Zealand and some other countries, such as Australia are much less acute than those which prompted the relatively limited form of co-ordination in the model law. It ought in principle, therefore, be possible to go further in respect of these countries. It should also be noted that the majority of situations of cross-border insolvency involving New Zealand companies involve Australian debtors and creditors.

### **Statement of the Public Policy Objective**

The objective for cross-border insolvency is to provide a modern, co-ordinated and fair framework to address, more effectively, instances of cross-border insolvency. The framework should enable businesses and individuals to act with certainty by providing a predictable regime, with low costs, for initiating cross-border proceedings.

### **Statement of Feasible Options (Regulatory and Non-Regulatory) that may Constitute Viable Means for Achieving the Desired Objectives**

There are no non-regulatory options that would allow for the implementation of an agreement to recognise a single cross-border insolvency proceeding.

Two regulatory options have been considered for achieving the desired objective:

- Implementing the UNCITRAL Model Law on Cross-Border Insolvency (this has already been agreed by government and is being treated as the status quo); and
- Implementing the model law, with additional regulation to enable the implementation of agreements to recognise a single cross-border insolvency proceeding.

The Model Law establishes a procedure for co-operation between states in the event of a cross-border insolvency. Specifically, the law provides for:

- The rights of foreign representatives of insolvent entities to apply to local courts and for foreign creditors to participate in local proceedings;
- Recognition of foreign insolvency proceedings and representatives;
- Cooperation between courts and insolvency representatives based in different jurisdictions; and
- Rules that should apply to any concurrent proceedings.

The Model Law is procedural in nature and does not affect the substantive rules that will apply in a cross-border insolvency proceeding.

Option two provides for the adoption of an additional framework to allow the implementation of agreements for a single insolvency proceeding – which may have some effect on the rules that apply. The framework would provide for the following key modifications to the model law in respect of agreed countries and proceedings:

- Providing for immediate and automatic recognition of a specified proceeding as a proceeding that can be recognised in New Zealand;
- Precluding the commencement of a parallel local insolvency proceeding; and
- Conferring broad powers on the foreign representative in the proceeding to administer local assets and to distribute those assets to creditors.

This is the only option that would enable a requirement for a single insolvency proceeding in the event of a cross-border insolvency.

### **Statement of the Net Benefit of the Proposal, Including the Total Regulatory Costs (Administrative, Compliance and Economic Costs) and Benefits (Including Non-Quantifiable Benefits) of the Proposal, and Other Feasible Options**

The net benefits of adopting the UNCITRAL Model Law were outlined in an RIS when the government agreed to its implementation last year. The key benefits are greater legal certainty and predictable procedures for New Zealand businesses in accessing or initiating overseas insolvency proceedings and correspondingly, increased investment in New Zealand due to the reduced risks for investors should insolvency occur.

The recognition framework proposed would allow the government to implement a full mutual recognition agreement. A requirement for a single insolvency proceeding has the potential to further reduce the costs associated with cross-border insolvency proceedings, and to therefore increase returns to creditors. Specifically, costs associated with accessing foreign courts and seeking recognition under the model law provisions would be eliminated.

A potential cost of the implementation of agreements under the recognition framework is that parties to a cross-border insolvency may be required to ascertain their rights under the law of other countries. The extent of this cost is minimised through the requirement that a recognition agreement will only be implemented if the law in the other country adequately protects New Zealand creditors and debtors. This is only likely to be the case where the provisions of the foreign law are comparable to New Zealand provisions.

The extent of the costs and benefits outlined under both options will depend on the numbers of cross-border insolvencies involving New Zealanders. While there have been relatively few cross-border cases litigated involving New Zealanders, the increase in global trade and the number of cross-border transactions heightens the likelihood that cross-border insolvencies will occur.

### **Statement of Consultation Undertaken**

The Treasury, the Ministry of Justice, the Ministry of Foreign Affairs and Trade, The Inland Revenue Department, the Department of Labour, Te Puni Kokiri and the Department of Prime Minister and Cabinet have been consulted on the proposal in this paper.

Public consultation was undertaken on the proposal to adopt the UNCITRAL Model Law in 1999. The Ministry of Economic Development asked a series of consultation questions, including whether submitters considered there should be additional protocols established under the framework of the model law in respect of particular countries. There was support for the adoption of the law and the development of protocols under the law at that time from the full range of insolvency law stakeholders.

### **Business Compliance Cost Statement**

#### *Source of any Compliance Costs*

There will be a reduction in compliance costs for New Zealand businesses involved in cross-border insolvencies if a recognition agreement negotiated under the proposed framework is implemented. The reduction will occur because the agreement would:

- Eliminate the need for New Zealand creditors to apply to the foreign court for recognition; and
- Eliminate the need for New Zealand creditors to initiate a separate action in New Zealand in respect of insolvent entity.

Some additional compliance costs may arise for New Zealanders needing to ascertain the law of another country in order to determine the extent of their interest or claim.

#### *The Parties Likely to be Affected, by Sector and Size of Firm*

Both the reduction and additional compliance costs will affect New Zealand debtors, creditors and insolvency practitioners. It will have more of an effect on those debtors that transact across borders and those businesses that provide credit to businesses or individuals that transact across borders.

#### *Quantitative/Qualitative Estimates of Compliance Costs*

It is difficult to estimate the level of reduction in compliance costs for New Zealanders as the incidence of cross-border insolvencies is currently low and the nature of any mutual recognition agreement has not been concluded.

However, if agreements are negotiated, it could eliminate the need for New Zealand creditors to initiate separate action, either in New Zealand or another country, in relation to the New Zealand assets of a company from a country that is party to the agreement.

The extent of the reduction in costs could be significant, given that access to foreign courts would require access to counsel in that country and payment of court filing fees.

It is expected that any increase in compliance costs associated with learning the requirements of another country will be minimal. There are two factors that minimise these costs:

- The costs of learning another law may in any event be less than the costs of ascertaining the current law applicable to cross-border insolvencies, given the level of uncertainty that currently exists in the law; and
- A recognition agreement can only be implemented where the government is satisfied that the rules in another country adequately protect the interests of New Zealand debtors and creditors. If the laws of another country are significantly different, this test is unlikely to be met.

#### *The Longer Term Implications of the Compliance Cost for Business*

In the longer term, it is expected that mutual recognition agreements could be negotiated with a number of different countries. This would further reduce costs for New Zealanders involved in cross-border insolvencies.

#### *Assessment of the Risks Associated with any Estimates and the Level of Confidence that can be Placed on the Compliance Cost Assessment*

The compliance cost impacts will only occur if mutual recognition agreements are negotiated between countries. To date no such negotiations have taken place, however, Australian officials have indicated a willingness to consider such a proposal.

*The Key Issues Relating to Compliance Costs Identified in Consultation*

The public consultation undertaken on the UNCITRAL Model Law and possible protocols did not raise any specific compliance cost issues.

*Any Overlapping Compliance Requirements with Other Agencies*

There are no overlapping compliance requirements with other agencies.

*The Steps Taken to Ensure that Compliance Costs were Minimised*

Publicity about the insolvency law review measures will be undertaken prior to the implementation of new insolvency legislation. This will help to minimise any compliance costs that arise out of implementation of the measures.