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The Prime Minister
Level 8
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WELLINGTON

Dear Prime Minister

Introduction
I write this open letter to bring to your attention matters that I think are of national significance.

I undertake liquidations of companies. For the vast majority I act as a Court appointee at the petition of Crown agencies where the agency has been thwarted in its attempt to collect Government imposts. I have been doing this for about 12 years, however, for a variety of reasons, this is becoming untenable. If you wish to understand more about the predicament I suggest that you read a recent case, *Healy v Grant* CIV 2009-404-02279. This is available on my website.

The case is about a liquidator's fees. In the judge's commentary you will see that the liquidator's excessive charging is compared to my own. Many of the structural flaws inherent to our liquidation regime are discussed in the case.

The purpose of this letter is to explain what the problems are and what needs to be done about it. Before doing so I will explain the importance of liquidation to the Crown and give a brief overview of a matter I am currently working on to enable you to appreciate the circumstances.

Liquidation and the collection of Crown revenues
As you will know, much commercial activity in New Zealand is undertaken through companies. Where there is a corporate failure the Companies Act presupposes the existence of a liquidator to enforce redress. Such enforcement necessitates resources. A liquidator can be easily thwarted by the simple expedient of dispossessing the relevant company of assets prior to liquidation. This is not difficult as it usually takes a long time to put a company into liquidation by way of a Court order. Alternatively, the director / shareholders can very easily appoint a liquidator more amenable to their interest.

The Crown is severely disadvantaged in this process. I am personally aware of many, many millions which remain uncollected because of these structural impediments.

A current matter
I am the liquidator of a company called Ariya New Zealand Limited. In October 2008 this company was [redacted].

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The reason that the [redacted] is because there was a suspicion that it contained [redacted] from India.

In order to be benign I attempted a rescue of the company and its business. My pre-condition was that the company's tax liability was determined so that a suitable payment arrangement could be made. It turns out that the company had not filed tax returns for a number of years. The director had either destroyed the company's records or simply failed to give them to me. My estimate is that the company owes somewhere between $0.75 million and $1.5 million in tax. My estimate does not take account of the super-profits available in the sale of prohibited substances.

The director of the company is a [redacted] It would seem that he has been trading in [redacted] since 2003 [redacted] Whilst I was still trying to rehabilitate the company and its business, the director launched a pre-emptive attack on me. This entailed Court action and an accusation of extortion, communicated by his lawyer. Their case has disintegrated, but I still await the final formalities.

The director acknowledges owning substantial assets, a state of affairs not consistent with his failure to pay tax. Further, I was able to determine that he had prepared multiple sets of financial statements. The version of events given to his bank was very different to that presented to Inland Revenue. I reported this serious crime to the Registrar of Companies as I am legally bound to do, but did not even receive the courtesy of an acknowledgment.

As the Court action progressed its way through the Court system, I began to receive information from the local community, Mount Roskill. From more than one source I was told that the director was engaged in [redacted] and, more worryingly, for the purpose of [redacted] I have shipping documents in my possession that tend to support that suggestion.

In any event I have begun to investigate unexplained [redacted] The [redacted]. I have tried to follow the shipping documents. Despite the significant powers available to me under the Companies Act, I doubt I will succeed as I need to get information from countries such as Myanmar (Burma). They ignore me of course.

Meanwhile the director goes freely about his business, including overseas trips and the disposal of property. I have no power to stop him without undertaking significant litigation. I will do this, but it takes time. Had the Registrar of Companies acted upon my complaint there was a better chance of restricting his travel. I have, rather belatedly, sought help from the police. [redacted].

It may appear that I deal in the affairs of a small company with no national significance. Small it is, but the implications are significant. Not only has New Zealand adopted a system of self-reporting for tax, it has also done so for the importation process. The potential risks posed are enormous. [redacted].

[redacted]

More significant, perhaps, are other risks. Recall that the company was involved in the importation of [redacted] Again, these risks are managed by the maintenance and preservation of records which do not exist.

What I have described is a [redacted] I will now describe the supposed palliative for these ills followed by a series of policy suggestions.

Company law: the theory

Company law is premised upon the basis of good corporate governance. I would argue that the maintenance of appropriate records is crucial to such governance, including the formal preparation of financial statements. It is ironic that your Government has announced its intent to dispense with this requirement.

The theory is that the failure to adhere to appropriate governance standards triggers the retributive and compensatory consequences enshrined in the Companies Act. A liquidator is essential to the implementation of these measures. It is not working. The leaky building crisis is directly attributable to the failure of the theory underpinning the Companies Act with all the financial consequences that entails. Similarly, the finance company crisis has similar origins.

Even if successful at surmounting the hurdles of corporate law facing the liquidator, he or she then confronts the obstacles of trust law or, more recently for me, of trans-national money laundering. Even the corporate law stage is difficult because directors apply a scorched earth policy in dispossessing the liquidated company of any assets by which the liquidator could gain a toehold. In short, company law is failing and is in danger of collapse. This collapse is aided and abetted by a rogue element in the practice of law, an element that is endemic, threatening and pervasive. Aside from the paraphernalia of trust law, it cynically exploits and subverts those civil protections necessary to guard against injustice. In doing so, it will ultimately tear those protections down.

Suggested policy measures

Introduction

I believe that the State needs to urgently attend to four policy areas. These are:

- the reform of corporate law;
- the reform of trust law;
- the regulation of the practice of law and accounting profession; and
- the detection and prevention of money laundering.

I would not claim that the system is in imminent danger of collapse, though the building and finance company crises might suggest otherwise. I believe that, over the long term, an unnoticed slow burn can be just as devastating as a visible conflagration.

Reform of corporate law

My most radical solution is the repeal of the Companies Act in its present form. If the history of corporations is studied it can be seen that the company was never intended for the purpose to which it is now put. Limited liability was originally introduced by the Victorians to protect investors who had entrusted their moneys to others.

The problem that needed to be addressed was the circumstances in which there was separation between ownership and governance, where the owners could be held accountable for the sins of the governors in cases where they had no knowledge of or ability to control the risks being taken. Limited liability was not intended to encompass the circumstances where there is no separation. As the origins of the corporate form were forgotten English law was configured to introduce the notion of the closely held company. Simply, where there is no separation, there should be no inoculation against the effects of one's own decisions and actions. Corporate law should be reconfigured to avoid the phenomenon where an individual is insulated from the consequences of their own actions by the simple expedient of incorporation.

I accept that the closely held limited liability company is now too entrenched to be eliminated, in which case other reforms are necessary.

The first matter that requires attention is the manner in which a company can be incorporated. New Zealand is proud of the fact that it is the easiest country in which a company can be incorporated. It shouldn't be. I have seen many examples of companies under the control of one individual proliferating like algae blooms. These mazes make it practically impossible for a liquidator to hold the individual accountable.

Such companies are incorporated with virtually no capital. The reward belongs to the individual and the risk to the unsuspecting, unseeing creditor. The individual is safe in the knowledge that a liquidator will rarely have the stamina to pursue them for compensation. Still less is the likelihood that retribution will ensue. This state of affairs is significantly exacerbated by the misuse of trust law as I will detail below.

Any tightened procedure for incorporation should be accompanied by a warrant of fitness for directors. At the time of the original enactment of the limited liability statutes the Victorian parliamentarians were concerned that incorporation would result in a 'rogue's charter'. That is what we now have writ large. The warranting process should include declarations that make it easy to imprison offenders because punishment of this sort is almost unheard of, in marked contrast with the United States.

A third area of reform relates to maintenance of proper accounting records. Your Government is contemplating dispensing with a proper framework for accounting for small and medium sized enterprises. The Victorians introduced the notion of 'truth and fairness' in accounting to mitigate the effects of the limited liability 'rogue's charter'. Yet we set about dismantling this bulwark. Over the past 20 years I have endlessly made submission on this matter, to no avail. Your officials need to bear in mind that I have the practical knowledge of implementing the law, even if only with partial success.

The fourth reform relates to the burden of proof. In both civil and criminal proceedings the default position should be that the director has to prove innocence rather than the plaintiff having to prove culpability. Certainly, the failure to maintain appropriate records should be proof positive of malfeasance.

The fifth area of reform pertains to the process of liquidation. I am aware that it is belatedly proposed that liquidators are regulated. I have my reservations about the proposals. In any event, reform is urgent. Much more significant is the need to reinforce the rights of creditors. Parliament has recently made such amendment but it does not go far enough. The policy of allowing shareholders to appoint liquidators should be removed, particularly in closely held companies.

A sixth area of reform would be to encourage the use of third party funders. There is a thriving business in Australia in which moneys are pooled from investors and applied as loans to liquidators to fund litigation. Despite the doctrine of champerty and maintenance these lenders are operational in New Zealand. Indeed I have successfully used them myself. The difficulty is that these lenders are reluctant to operate in New Zealand because of the near impregnable walls created by the misuse of trusts and our dysfunctional personal insolvency regime. In short, there is no point in having a cast iron case at the level of company law only to be defeated by our personal insolvency law.

At least as importantly, the legal processes which confront the liquidator need reformation. One idea that has been suggested to me is that there be established a dedicated insolvency court. That might introduce more efficiency and speed. However, this is not sufficient.

The court processes themselves need to be reformed. There should be an imperative to mediate or arbitrate early in the process and I understand this is about to happen. Further, the full paraphernalia of legal manoeuvering, such as the perpetual interlocutory application, should be curtailed. In the specific matter I raised at the outset, this process has been wholly abused to attack me. Whether the intent or not, the attack has the effect of consuming finite resources.

The role of the legal profession

This brings me to the role of the legal profession. Typically how the process works is this. The insolvent, liquidated company has been gutted before the liquidator arrives. The record trail is either deliberately or inadvertently rendered opaque. The ill-gotten gain is then deployed to hire a lawyer. The lawyer uses the all of the sophistry and complexity of the law to thwart the liquidator. The director is indifferent to the applications of the moneys. They prefer the moneys be pocketed by the lawyer than the liquidator or the creditor. Win, lose or draw the lawyer is enriched with impunity.

How can this be addressed? I am aware of the recent reformation of the law governing the practice of law. However, the system remains self-regulatory. I have no confidence in such regulation. The phenomenon of 'there but for the grace of god go I' prevails. I have long standing experience of the law society and its disciplinary process. It was an abject failure then. I see no reason why this won't continue.

One of two measures can be employed. Firstly, any money that is available to the defendant in a Companies Act matter should be put into a pool so that both protagonist and antagonist should share it. Secondly, the lawyer should be on notice that if they lose they should be compelled to return their fees plus interest. In addition I think a substantial levy should be imposed for incorporation, the lion's share of which should be paid to the liquidation surplus account – a public fund for the purpose of funding liquidators.

Ultimately, these measures are no substitute for persons who have been granted privilege, such as the right to represent in court or operate the banking system, to understand their wider duty to society. A deep and intensive ethical training is necessary.

Dame Margeret Bazley's recent study of the practice of criminal law struck a resonating chord with me. Perhaps a practical measure would be to extend her study to consider the practice of civil law. Its misuse is as pernicious as that which she describes in respect to criminal law and is, possibly, more insidious.

The misuse of trusts

I now turn to the misuse of trust law. Trusts are essential. Estates arising on death could not be administered without the testamentary trust. However, I see no real societal benefit for the *inter vivos* trust, though I declare an interest as I am a party to one. A reform in this area is simple. If a person habitually uses an asset, that should be sufficient to found an ownership interest. These assets should be able to be realized for the benefit of a delinquent's creditors.

The misuse of trusts has been introduced into the operation of the corporate form. The intent is to create an extra layer of insulation against accountability. It can be shown that this is ineffective, but this is not well understood. Because it is not well understood an additional burden is imposed on a liquidator carrying out his or her duties. The solution is simple: the practice of corporations as trustees, except in limited circumstances, should be outlawed.

An associated problem is the inefficacy of our current personal insolvency regime. As you will know the stories of wealthy malefactors maintaining their mansions are legion. I do not understand why the State maintains a monopoly on personal insolvency. In other countries this work is carried out by the private sector. I am certain the introduction of economic motive will greatly enhance the effectiveness of the personal insolvency regime. I would have thought this entirely consistent with your views – if there is a private sector solution to any given problem, the State should withdraw.

Money laundering

I think an area of policy that urgently needs to be addressed is money laundering. I have not encountered this before and I am surprised how impotent I am when confronting it. I have begun to deploy my legal powers to seek information. I do not know yet whether I will be successful. I am not, however, optimistic. As noted, one of the countries from whom I seek important information is Myanmar.

There is more than sufficient law in place now to deal with this matter on a retrospective basis once it is detected. The need is for both the enhancement of detective measures and for prospective measures. That is, there needs to be some central data base readily accessible for the authorities. This is the matter about which you should worry most. The ease with which New Zealand can be used for the transmission of money has serious implications for the revenue gathering agencies, amongst others. How long will it be before New Zealand is seen as the soft target? Perhaps it already has been. I doubt anybody knows.

Plea for help

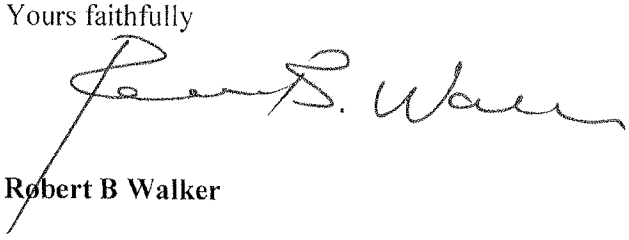
There is no time for complacency. I recently had to watch a diligent colleague dragged through the courts to defend his fees. In a conversation with him I made reference to the work he carries out on behalf of the State. To my great consternation he intimated that he wasn't interested anymore. The civil service needs to be properly resourced and coordinated amongst agencies with Inland Revenue in the vanguard. There is, I admit, an element of the self-serving in this suggestion. However, I feel much the same way as my colleague. The skills I deploy in the field can easily be deployed elsewhere.

I have a deep sense of indignation about the current matter I described. This is caused by people who accept our hospitality and compassion and then set about pillaging our country. The rule of law is precious. Its slow erosion will have devastating effects in the long term. But for parliamentarians this lesson is paramount. Do not enact laws that the State, directly or indirectly, has no will or ability to enforce. Better no laws than law as token.

At the moment you, as the head of Government, are desperate for revenue. I personally know that you are missing out on millions and millions because of our dysfunctional insolvency regimes.

I will happily discuss these matters with you or your officials if you wish.

Yours faithfully



Robert B Walker