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LAWYERS

Fineprint

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Protecting Shareholder Advances and Guarantees

All too often shareholders overlook the need to properly secure the advances they make to their company, or the guarantees they grant in favour of their company, without being aware of the consequences that can result from this oversight. By registering security over the assets of their company, shareholders can effectively and efficiently secure their advances to that company and feel assured that steps have been taken to safeguard their investment.

If you're a business owner, you should endeavour to structure your affairs in a manner that reduces risk. As part of mitigating your risk, it's important you understand that when you advance funds to your company, or grant guarantees for the benefit of your company, you're just as entitled as any other creditor to take security.

No one starts a business with the mindset that it will fail and, in the normal course of business, shareholders shouldn't need to call upon their security. However, circumstances change and if a company faces financial pressures or is put into liquidation or receivership, the shareholders may need to shift their focus to preserve their position ahead of the company and its creditors.

What is a shareholder advance?

Shareholder advances encapsulate all loans that a shareholder makes to their company. Whenever a company is incorporated, or a company requires more working capital, it's likely that its shareholders will lend funds to the company, whether by way of a term loan or through a shareholder current account. Both of these methods of lending to the company are considered to be shareholder advances and should be secured against the assets of the company.

Why register a security?

As a shareholder, when you register a security with respect to your advances, you become a secured creditor of your

company. By becoming a secured creditor, you will rank ahead of all the company's unsecured creditors, increasing the likelihood that your shareholder advances will be repaid if the company becomes insolvent.

There's nothing improper or immoral in you establishing a priority position in this manner. Other creditors have the right to search for shareholder security on the Personal Property Securities Register to determine who is ranked ahead of them. Creditors also have the right to demand security from a company or to rearrange the priority of various securities, before they sell goods to a company on an unsecured basis.

An additional and often overlooked benefit of securing shareholder advances is that by being a 'secured' creditor, you will have a greater degree of influence over liquidators and receivers – which is important at a time where shareholders and directors often have very little or no influence over their company.

Guarantees

Outside of the insolvency context, a well-drafted security agreement will also allow you to have recourse to the assets of the company in the event that a guarantee you enter into for the benefit of the company is enforced. Where you have given a shareholder guarantee to a creditor (usually a bank), it's not uncommon for a creditor to call upon the shareholder guarantee without first taking action against the company if the company cannot immediately pay. This is particularly relevant where the creditor has recourse to property held by the shareholder. In this situation, it is important that if you're the affected shareholder, you can legally and efficiently seek recourse against the company as compensation for your loss.

Preparing and registering a general security

Security for shareholder advances often takes the form of a general security over all of the company's present and after acquired assets. This security is recorded in a general security agreement (GSA) that's signed by the company.

The preparation of a GSA is relatively straightforward, meaning that the time and cost involved with instructing a lawyer or accountant to draft a GSA is insignificant when compared with the protection a GSA provides.

Once a GSA has been prepared, it's essential that the security described in the GSA is registered on the Personal Property Securities Register (often referred to as the PPSR), which is administered by the New Zealand Companies Office. The PPSR is the register where details of security interests in personal property are registered and can be publically searched.

The timing of the registration of your security is very important. Generally, the order of registration determines the order of priority between secured creditors – so it's critical to register your security as soon as possible.

Other practical considerations

Ideally shareholders should register their security arrangements before advancing funds to their company, no matter how healthy the business is at the time of the advance. Often shareholders only consider taking security when their company is already in financial difficulties. If the company is finding things tough financially and a shareholder registers a security should that company subsequently be placed into liquidation, the liquidator operating under the Companies Act 1993 regime will likely render the security taken by the shareholder as voidable. This means that the shareholder will end up being an unsecured creditor.

In addition to relying on shareholder advances, many companies will have borrowings with banks and lenders, which will often be secured by a GSA or other security arrangement in favour of the lender. It's important that you check the provisions of the lender's security before registering a shareholder security, as the terms of the lender's security may prohibit the creation of further security interests without their consent. Consent from an external lender should be obtainable as long as they can be assured that the obligations owed to them are sufficiently secured. Some lenders may require a deed of priority in this situation to provide sufficient comfort that the shareholders' security will rank behind the lender's security.

Exit of a shareholder

In addition to securing shareholder advances, if you're a shareholder in a multi-shareholder company, you should also turn your mind as to how shareholder advance/s will be repaid if another shareholder exits the company. Although many shareholders' agreements address what will happen to a shareholder's shares on exit, often no thought is given to repayment of shareholder advances. We recommended that shareholders get advice about the range of options available to cover repayment of shareholders' advances, and releases of guarantees on exit.

In summary, for minimal cost and no matter how healthy the company is at the time you make a shareholder advance to your company or provide a guarantee, you should always secure that advance and/or guarantee by taking security over the assets of your company. By becoming a secured creditor, you can give yourself the best chance of protecting your investment and maintaining as much control as possible in the event of a liquidation. ■

Changing Landscape in the Workplace

New health and safety legislation comes into force in early April

Organisations should always be aware of their obligations and responsibilities regarding health and safety. This is even more so now as new law, the Health and Safety at Work Act 2015, comes into force on Monday, 4 April this year. A summary of the most significant changes is set out below. We follow this with some practical steps to take to give you and your organisation the best chance of complying with the new legislation.

The new legislation imposes an enhanced primary obligation on a PCBU (Person Conducting a Business or Undertaking) to take 'reasonably practicable' steps to ensure the health and safety of their workers. PCBUs include employers, principals, self-employed, partnerships and other people who manage or control a workplace. However, if you or your organisation don't have any employees then you will not be considered to be a PCBU.

The new duty

If you are a director of a company or an officer you are required to exercise due diligence to ensure compliance with the new Act. Officers include those who hold positions that allow them to exercise significant influence over the management of a business. 'Due diligence' involves taking reasonable steps to:

- Acquire and keep up-to-date knowledge of work health and safety matters
- Gain an understanding of the nature of the operations of the business and generally of the hazards and risks associated with those operations
- Ensure that the PCBU has available for use, and uses, appropriate resources and processes to eliminate or minimise risks to health and safety
- Ensure that the PCBU has appropriate processes for receiving and considering information regarding incidents, hazards and risks and responding in a timely way to that information
- Ensure that the PCBU has, and implements, processes for complying with any duty or obligation, and
- Verify the provision and use of necessary resources and processes.

The purpose of the due diligence requirement for health and safety compliance is for directors and officers to take a more hands-on approach to health and safety.

Defining the workplace

Earlier drafts of the new legislation originally defined 'workplace' in a manner viewed by commentators as being too wide. However, adjustments have been made in order to appease those who were concerned, particularly farmers. 'Workplace' will now be defined as where work 'is being' or 'is customarily' carried out. This means that the duty of a PCBU in a farming context would not apply to the main dwelling house or to areas of the farm other than farm buildings unless work is being or is customarily carried out at that place.

Investigations, recording and notifying

There are new requirements on PCBUs to carry out internal health and safety investigations into incidents and, in some circumstances, to provide the findings of those investigations to a health and safety inspector. The purpose of an investigation is to identify and address contributing factors to prevent the incident happening again. In addition, there are new obligations concerning the recording and notifying of workplace accidents and serious harm.

Practical steps

The new Act will soon be in force. You should therefore:

- Familiarise yourself with the new legislation
- Understand your position under the new Act
- Review and update the current approach to health and safety of your organisation, business or company
- Inform your workers
- Talk with us if you need to, and
- Above all, don't leave it too late.

This new legislation increases the penalties for non-compliance and creates a new three-tiered hierarchy of offences.

1. Reckless Conduct: fines up to $3,000,000 or $600,000 and/or up to five years' imprisonment for individuals
2. Failure to comply with a duty exposing risk of death or serious injury/illness: fines up to $1,500,000 or $300,000 for individuals, and
3. Failure to comply with a duty not exposing death or serious injury/illness: fines up to $500,000 or $100,000 for individuals.

If you're unsure about these changes or how you and your organisation will be affected then please don't hesitate to be in touch with us. ■

Are We in a De Facto Relationship?

If you are in a de facto relationship, there could be significant financial implications for you if you separate, or if your partner (or you) dies

The principal piece of legislation which deals with the division of property belonging to couples or married couples is the Property (Relationships) Act 1976 (the PRA). Substantial reforms in 2001 extended the scope of the PRA to cover de facto relationships. But what exactly constitutes a de facto relationship in the eyes of the law?

The PRA states that the basic criteria for a de facto relationship are:

- There must be a relationship between two people
- The relationship maybe heterosexual or homosexual
- Both parties must be aged 18 years or over
- They must not be married to each other, although they may be married to someone else, and
- The parties must *'live together as a couple'*.

Living together as a couple

The PRA sets out a list of matters to be taken into account in considering whether two people 'live together as a couple'. These matters are:

- The duration of the relationship: the longer that two people have been associated together, the more likely it is they will be found to be living together as a couple
- The nature and extent of common residence: two people may live together (in terms of the PRA) even if they do not reside at the same address. But the more time they spend together at the same place, the easier it will be to regard them as a couple
- Whether a sexual relationship exists
- The degree of financial dependence or interdependence, and any arrangements for financial support between them
- The ownership, use and acquisition of property: co-ownership, particularly of the common residence, is a sign of living together as a couple. The same can be said of using property in common, such as a car, and buying items together
- The degree of mutual commitment to a shared life: commitment is an important test of whether there is a de facto relationship. Certain objective criteria such as a common address is important, but there must also be a subjective element of their commitment to a shared life
- The care and support of children: where two people have a child it does not follow that they are necessarily de facto partners. However, children of a relationship will often be relevant in identifying a further level of commitment by the couple
- The performance of household duties; for example, the sharing of domestic duties may indicate a commitment to a shared life, and
- The reputation and public aspects of the relationship; if two people appear together in public and attend events together as a couple this can provide evidence they are a couple.

This is not an exclusive list; any other circumstances can be considered. There will be situations where some circumstances are more relevant than others. Also, no one specific factor is a necessary condition to determine whether or not there is a de facto relationship.

There have been cases where the court has found there to be a de facto relationship even though the two people are not residing together. That said, whilst cohabitation isn't *absolutely* necessary for a de facto relationship to exist, it is a very persuasive factor.

What is not a de facto relationship?

Various relationships can easily be identified as falling outside the definition of a de facto relationship. For example, a boyfriend/girlfriend relationship where both people have independent lives and do not cohabit does not have the hallmarks of a de facto relationship, even if it is a close, personal and sexual one.

If two people's relationship is not a de facto relationship (or they're not married or not in a civil union) they fall outside the scope of the PRA. If these people have issues relating to property, they must therefore use some other legal remedy to try to resolve their property-related dispute.

The question that often arises in these cases is just when a relationship shifts from being a more casual type of relationship to a qualifying de facto relationship to which the PRA applies. In each case, that will involve a detailed consideration of the above factors, and possibly others.

How we can help

If you need further advice about how the PRA could apply to you, and possible steps you may be able to take to contract out of it, please be in touch. ■

Cyberbullying – stopping the trolls

In recent years there has been a significant increase in online abuse particularly of vulnerable young people. A high profile example was the 2013 'Roast Busters' case involving teenage boys bragging of sexual activities with girls. This article looks at what remedies are available when cyberbullying takes place.

Cyberbullying has become commonplace with dreadful consequences for the victims including depression and suicide.

In September 2015, a 24 year-old-man was arrested in Denmark after a joint investigation between New Zealand and Danish authorities. The man posted private photos of an Auckland schoolgirl on websites and subsequently hacked the computers of the girl's family and school.

New legislation will help

The Harmful Digital Communications Act 2015 came into effect on 1 July 2015. It aims to deter and prevent harm from digital communication and to provide victims of harmful communication with a means of redress. The definition of 'digital communication' includes posting on the internet and social media sites, and phone communications such as texts.

It's now an offence to post a digital communication that causes harm to a victim, if the post is intended to cause harm and if an ordinary reasonable person in the victim's shoes would have been harmed.

Since the Act came into force eight people have been charged and, to date, three have been convicted. The most recent conviction involved a Christchurch man sending numerous threatening images and messages to his former boss.

The Act provides limited protection from liability to websites (such as Facebook) that might host harmful content. However, the host must comply with certain procedures. It must be easy for users to make complaints. Any complaint must be forwarded to the author of the post and, unless the author objects, in most cases the post must be removed within 48 hours of the complaint.

The balance of the Act (coming into force on a date to be decided prior to 2 July 2017) contains additional remedies for victims. The legislation will establish a statutory agency to receive and investigate complaints about harmful digital communications.

If the agency cannot negotiate the removal of a post or has not deterred someone from posting on websites, the District Court will have the power to make various orders including that specific content be removed, that conduct be stopped, or that a correction, apology or right of reply be published.

These orders can be made against the original poster as well as the website host. If necessary, the court can order that the identity of an anonymous author be revealed to the court. This is aimed to stop those people, commonly known as 'trolls', who hide behind the internet to hurl abuse at others safe in the knowledge that no one knows who they are.

Commentators acknowledge the Act addresses an important and real need – protecting the vulnerable and limiting harmful behaviour. Critics fear unjustified complaints could be used to unfairly target a person, publication or field of discussion and limit freedom of speech.

Most people would agree that the law needed to address issues with cyberbullying. Time will tell whether the changes are effective. ■

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Postscript

Computer virus scams

There can be very few of us who have not been rung with the caller saying they've noticed your computer has a virus. They give you directions on where to look on your computer, and then helpfully suggest that you download some software and sign up to a service that is meant to keep your computer safe.

And of course there is no virus, but you've lost your money and your computer may have been hacked.

To protect yourself from computer virus scams, the Ministry of Consumer Affairs has some advice:

- If someone calls you to say your computer has a virus, simply hang up the phone – even though your mother always told you that was rude.
- If the caller becomes aggressive or unpleasant, don't talk back, just hang up the phone.
- As a result of the scam, if you've already downloaded some software, immediately unplug your computer from the internet.
- You should also run spyware and antivirus programs and change all your passwords, using a different computer. If in doubt, take your computer to a technician to be 'cleaned'. And don't use it in the meantime.
- If you've signed up to a service contract which you believe to be a scam, contact your bank or credit card provider immediately. You may be able to get a chargeback. ■

Getting organised for a new employee

Planning for a new employee isn't just making sure they have a desk and chair. The Ministry of Business, Innovation & Employment (MBIE) has compiled a checklist for employers to carry out before your new person starts. Not only does being prepared make your new employee feel more welcome, but it also makes them more efficient from Day One.

1. Set up equipment: Have a desk and chair ready, business cards and stationery, telephone, car, toolkit, safety equipment and so on.
2. IT: Get passwords and access, as well as an email address, arranged the week before.
3. Tell your insurance company: your insurer will want to know you've a new employee. It's all about protecting your business.
4. Establish an employee file: This is required by law. Amongst other things it will contain your offer letter, the signed employment agreement, emergency contacts, visa details if relevant, etc
5. Payroll: You'll need their IRD number, KiwiSaver details, bank account number, tax code, etc so you can set up your payroll in good time.
6. Share your company policies: It's important that your new employee understands your company policies (start and finish times, breaks, annual leave, etc) and adheres to them.
7. Health and safety: It's vital that your new employee is aware of your health and safety practices, understands safety procedures around equipment, knows the evacuation procedures, etc.
8. Workplace equipment and tools: Ensure there's access to the tools and equipment they need to do their job, ensure they have swipe cards and so on.

MBIE's website is very business-friendly, check it out at www.mbie.govt.nz ■

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