

BURROWES and Company



Barristers and Solicitors

Client Newsletter

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DISCLOSURE OBLIGATIONS FOR INVESTMENT ADVISERS AND BROKERS

Over the past 2 years, more than 25 finance companies have either failed completely or run into some kind of trouble. New legislative measures, in the form of the Securities Markets Amendment Act 2006 and the Securities Markets (Investment Advisers and Brokers) Regulations 2007 and 2008, impose disclosure requirements on investment advisers and brokers to ensure that investors are better informed. The Act and Regulations are now read into and/or alongside the Securities Markets Act 1988.

The Duty to Disclose

The Act and Regulations impose upon investment advisers and brokers an obligation to disclose certain information before providing investment services. The disclosure must be made in writing and must be provided up front. The information required to be disclosed by advisers and brokers is different, with the advisers' disclosure obligations having a wider scope.

Investment advisers must disclose information relating to experience; qualifications and professional standing; certain criminal convictions; fees; other interests and relationships; and the types of securities about which the adviser gives advice.

Investment brokers must disclose certain criminal

convictions and procedures for dealing with investment money and property.

One point of interest is the requirement for Investment Advisers and Brokers to disclose their commission structure and the amounts before advice is given. This includes all remuneration that the adviser or broker may receive following the giving of advice.

Criticisms

The Regulations have been criticised because advisers and brokers are not required to give advice about the nature and quality of the investment and the client is not required to sign any agreement or receive any warning about associated risks. It has been suggested that a client agreement setting out risks associated with the investment ought to be a requirement.

CONTRACTING WITH YOUNG PEOPLE

Case Review

Wine Country Credit Union v Rayner and Anor, 2008, HC Napier, (CIV-2007-41-00016)

Background

R and T (both minors) borrowed \$15,612 from WCCU to purchase a car. R was apprehended driving the car without a licence and the Police impounded the car. It was repossessed by WCCU and resold, leaving \$12,000 owing on the loan. WCCU sued R and T for the outstanding \$12,000, but were unable to recover it. Both the District and High Courts found that the contract could not be

enforced against R and T because they were minors when they entered into the loan contract. R was 17 years and 9 months and T was 17 years and 6 months at the time of entering into the contract.

The Minors Contracts Act 1969

Under the Minors Contracts
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AVOIDING EXTRA COSTS WHEN BUILDING

In a recent article in *MG Business*, Chris Hutching discussed contracting to build a new home (whether for investment purposes or residential), and expressed concern about particular payment arrangements that can leave owners out of pocket.

Hutching recommends when buyers are required to pay a deposit direct to the builder, that this is paid into an independent trust account, rather than paid out directly. This provides the buyer with some protection in the event that the development stalls or the building company or building developer goes bust.

Another payment issue to be wary of is progress payments. Buyers (and their advisers) should endeavour to link the value of progress payments to the value of the work being done at each stage. Where progress payments are forward loaded (greater at the start of the contract although the value of the work at that stage might be comparatively less than other stages of the build), buyers can often have to find more money to complete the build.

The buyer's contract should set out clearly what payments are due, who they are to be paid to and on what basis. Payments should be linked to the costs incurred at each stage of the build and not just be made as payments for percentage of completion.

CONTRACTING WITH YOUNG PEOPLE

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Act 1969, contracts other than certain contracts for life insurance and contracts of service are presumed unenforceable against a person under 18 years of age. The Court may, however, in its discretion, enforce all or part of a contract against a minor where it is "fair and reasonable" in all the circumstances to do so.

Application in this Case

In this case the Court did not find circumstances that would make it "fair and reasonable" to enforce the contract against R and T. The Court found that WCCU's enquiries had been inadequate both in terms of establishing the ages of R and T and in establishing their ability to repay the loan. R and T had not deliberately misled WCCU, rather, they had stated their dates of birth truthfully on the loan application. An employee of

WCCU had incorrectly calculated their ages as being over 18.

Conclusion

The error in calculating R and T's ages and the failure to question them about fundamental aspects of their application led to WCCU losing \$12,000 and incurring the costs of litigation. The case serves as a reminder of the importance of checking the age of a young person you are contracting with and to be aware that if they are under 18 the contract may not be enforceable against them.

SHAM TRUSTS

Case Review

Official Assignee in Bankruptcy (in the property of Reynolds) v Wilson & Ors [2008] NZCA 122.5

Background

This case concerned a bankrupt property developer, Mr Reynolds. Mr Reynolds had first been bankrupted and discharged in the 1990s. In 1996 he established a family trust and settled the family home into the trust. In 1998 the family moved, and this new property was settled into the family trust also. In 2001 Mr Reynolds was bankrupted for a second time and there were no assets to administer.

Administration of the Trust

The Court found that the trust "was never administered very well" and that "there was intermingling and confusion between the affairs of the trust and Mr Reynolds, at a personal level and even in the record keeping of his solicitor's trust account." The Official Assignee argued that the trust was a sham, or otherwise that the trust was Mr Reynolds' alter ego.

Sham and Alter Ego Trusts

A sham trust arises where there is an intention by the settlor and the trustee (and these might be the same person) to establish a trust in appearance only. A sham trust requires the intention to deceive.

An alter ego trust arises where a person has such control over a trust that the trustees are considered to be mere puppets of the controller. The trust is a genuine trust, and there is no intention to deceive.

Court's Discussion of Trusts

In regard to Sham Trusts, the Court concluded that the intention to deceive is to be assessed subjectively – that is, it will look at the actual intention of the settlor and trustee, not just to the appearance of the trust. Justice Glazebrook stated that "after all, the whole point of a sham is that it is intended to have an effect other than the effect it would have if looked at objectively".

The lesson here is that, in establishing a trust, it is not merely a question of using the right process, but also having a genuine intent in relation to the establishment and use of the trust.

As to alter ego trusts, the majority of the Court concluded that alter ego trusts are not an independent cause of action, but only evidence to help establish a sham trust. So the effective control of the trust will not necessarily leave the trust open to attack, but may be evidence used in that process.

LIMITED PARTNERSHIPS

The Limited Partnerships Act 2008 ("the Act") came into force on 2 May 2008 and replaced the special partnerships provisions of the Partnerships Act 1908. The Act has established a new regulatory and tax regime for limited partnerships intended to "give the business community in New Zealand the option of a flexible and internationally recognised business structure similar to limited partnerships in use in overseas jurisdictions" and to "facilitate the development of the venture capital industry in New Zealand."

Features of a Limited Partnership

A limited partnership is a separate legal person. It must be made up of at least one general partner and one limited partner who cannot be the same person. Subject to this requirement, there may be any number of general or limited partners.

'General partners' are responsible for management, whereas 'limited partners' must not take part in the management of the limited partnership. Either type of partner (subject to the partnership agreement) may, but does not have to, make a capital contribution to the limited partnership. If a limited partner becomes involved in managing the limited partnership, they lose the

protection offered by their limited partner status, and become liable for the debts and liabilities of the limited partnership. The Act provides a schedule of activities that will not constitute taking part in the management of the partnership, so limited partners can take certain actions with the confidence that their limited liability status will be maintained.

The limited partnership must have a written partnership agreement as to the affairs of the limited partnership and the conduct of its business. On registration the partnership agreement will be binding upon the partners - although it will be ineffective to any extent that it contravenes or is inconsistent with the Act.

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UNIT TITLES

The Unit Titles Bill ("the Bill") was introduced into Parliament on 29 May 2008 and, once passed, should make a range of positive changes to the Unit Titles Act 1972. The proposed changes clarify ownership and responsibility issues; change voting requirements and require bodies corporate to establish a long-term maintenance fund.

Under the Bill, the body corporate will own the common property and the definition of 'common property' will be broadened to include building elements that affect more than one unit. This will allow the body corporate to act for the benefit of all owners in terms of maintenance and repair, and will mean, for example, that a leaky roof would be the responsibility of the body corporate to repair rather than the owner of the top floor apartment.

The Bill will remove the need for unanimous body corporate decisions. The voting requirement will be changed to 75% of those who vote, which aims to reduce the risk of "holdouts" and the ability of those who do not vote to hold up the workings of the body corporate. There will, be new processes to ensure minority views are heard.

Bodies corporate will need to establish maintenance plans of at least 10 years and a long-term maintenance fund. This should allow unit owners to keep maintenance costs stable over time and should ensure that funds are available for unforeseen maintenance expenses.

Large, staged or mixed-use developments will be able to be 'layered' into subsidiary units within a unit title development. These units will have their own body corporate, and each of those subsidiary bodies will be members of the head body corporate. For example, a development including an apartment block, shopping centre and car park building could have three subsidiary bodies corporate to manage the different interests of each group of owners.

CLIENT CARE

New legislation regulating lawyers came into effect on 1 August 2008. As a result we have adopted a client care charter and a copy of this has been enclosed with this newsletter. The purpose of the new regulations and of our charter is to ensure that whenever you are receiving legal services from us, you are aware of your rights and of what to do if you have queries or complaints.

If you do have queries or concerns about any aspects of our services please contact the person handling your file or Michael Burrowes directly. If you would like more information on our client care charter please contact us.

NEW REQUIREMENTS FOR SOCIETIES

Incorporated societies are now required (as of 1 June 2008) to provide evidence that financial statements have been submitted and approved at a general meeting of the society. The evidence is to be submitted by way of a certificate. Financial statements that are not certified will be rejected by the registrar. The Financial Statement Coversheet for an Incorporated Society form is available at the societies website www.societies.govt.nz.

The form is a simple one-page document and it provides the basis of certification. Societies are then able to file their annual financial statements (along with certification) either online at the societies website, or by post.

COMMERCE COMMISSION WARNS: IT'S NOT EASY BEING GREEN

With rising fuel prices and increased awareness of our 'carbon footprint', being Green has become all the rage – or perhaps more appropriately - all the envy.

It should come as no surprise then that advertisers have pounced upon what is being dubbed 'greenwashing' as an essential tool for marketing.

Indeed some have taken to it with such fervour, that in their bid to out-green the competition, the accuracy of the claims have been left wanting.

This has become a focus for the Commerce Commission who in issuing warnings recently, noted that the "growing trend of greenwashing by businesses is cause for concern if the green, eco-friendly or sustainability claims are false or misleading".

The Commission will be keeping a close eye on the issue, and where necessary, enforcement action will be taken under the Fair Trading Act.

All information in this newsletter is to the best of the authors' knowledge true and accurate. No liability is assumed by the authors, or publishers, for any losses suffered by any person relying directly or indirectly upon this newsletter. It is recommended that clients consult a senior representative of the firm before acting upon this information.

FLEXIBLE WORKING ARRANGEMENTS

The Employment Relations (Flexible Working Arrangement) Amendment Act 2007 came into force on 1 July 2008. To request a flexible working arrangement, a person must have been employed by their employer for the immediately preceding 6 months and must have "care of any person".

What can employees request?

An employee can request changes to their hours, days, and place of work. A request must specify whether the variation would be permanent or for a period of time, when the employee proposes that the variation would take effect, and (if for a fixed period of time) the date at which the variation is to end. Employees must also explain, in their view, how the variation will enable them to provide better care for those they are caring for and what changes, if any, may need to be made to their employment arrangements if the request is approved.

How Employers Are To Deal With Requests

An employer must approve or refuse any request "as soon as possible", but no later than 3 months after receiving it. The listed grounds for refusal are: inability to reorganise work among existing staff; inability to recruit additional staff; detrimental impact on quality; detrimental impact on performance; insufficiency of work during the periods the employee proposes to work; planned structural changes; burden of additional costs; and detrimental effect on ability to meet customer demand. A request can be refused because of one of the grounds listed above, ineligibility, or both.

An employer is required to refuse a request if the employee is bound by a collective agreement that covers working arrangements and the requested new arrangements would be inconsistent with that. The employer must notify the employee of the ground for refusal and provide an explanation for it.

Challenging Refusal

A challenge may only be based on an employer's alleged failure to comply with the regime's procedural requirements, not on whether the end decision was reasonable. If the Employment Relations Authority finds that an employer has made a wrong determination as to the eligibility of the employee to make a request, then it can require the employer to reconsider the request as soon as possible. If an employer fails to comply with the procedural requirements of the Act, it is liable to a penalty of up to \$2,000, payable to the employee.

LIMITED PARTNERSHIPS

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Limited partnerships have 'flow-through' tax status, meaning partners will be taxed individually at their personal tax rate rather than the partnership being taxed as a whole.

Searchable Register

The Companies Office administers the Limited Partnerships Act and provides a searchable register of New Zealand Limited Partnerships and Overseas Limited Partnerships that are conducting or engaged in business activities in New Zealand. The register is available on the Companies Office website at www.companies.govt.nz. While information relating to the limited partnership and the general partners are available, the Registrar treats information on limited partners as confidential, and must

not make it available to the public.

Encouraging Investment

Limited partnership regimes are found in countries including Australia, the United Kingdom, Canada, Singapore and the United States where they are a preferred structure for investing in venture capital. The Act should allow New Zealand businesses to compete for capital in this market, and this is particularly important for new businesses.



CLIENT CARE CHARTER

New legislation regulating lawyers commenced on 1 August 2008. As a result we have adopted a Client Care Charter.

Whenever you receive services from us, we will:

- act competently, in a timely way, and in accordance with instructions received and arrangements made;
- protect and promote your interests and act for you free from compromising influences or loyalties;
- discuss with you your objectives and how they should best be achieved;
- provide you with information about the work to be done, who will do it and the way the services will be provided;
- charge you a fee that is fair and reasonable and let you know how and when you will be billed;
- give you clear information and advice;
- protect your privacy and ensure appropriate confidentiality;
- treat you fairly, respectfully, and without discrimination;
- keep you informed about the work being done and advise you when it is completed; and
- let you know how to make a complaint and deal with any complaint properly and fairly.

The obligations lawyers owe to clients are described in the Rules of Conduct and Client Care for Lawyers. These obligations are subject to other overriding duties, including duties to the courts and to the justice system.

If you have any questions, please visit www.lawsociety.org.nz or call 0800 261 801.

1 August 2008