Protect your business from bad debtors

Owners or managers of small to medium sized businesses will be increasingly aware of how the global credit squeeze is affecting New Zealand. As finance companies collapse, fuel costs escalate and interest rates rise (amongst other things) the pressure grows for everyone to cut costs and make savings. One common response from debtors to these pressures is to delay paying creditors – including you. Effectively they are using you as a low cost source of extended funding.

Planning how best to protect your business from bad debtors involves both practical and legal issues, as set out in the following paragraphs.

Take time at the outset to ensure the customer can and will pay. Sometimes the promise of a new order for work overrides common sense enquiries at the time about the customer's circumstances and their ability and willingness to pay the price you require.

Ensure that you have full details of your customers before you commit to the work. This includes all of their contact details but also the legal name and type of entity. All too often creditors go to take enforcement action only to find they are missing details that compromise debt recovery. For example, you might assume your customer is John Brown trading as John's Timber Supplies only to find out that he was representing John Brown Limited trading as John's Timber Supplies. This can result in you having no action against John Brown personally, only his limited liability company, which might be insolvent.

If your customer is a small company, obtain a guarantee from the directors. It is often more effective to pursue a director personally, rather than a company.

Have written terms of trade that the customer signs before you supply the product or service. This makes it very difficult for the customer to dispute your terms at a later stage, which often happens if the terms are posted with an invoice, after supply, or not recorded in writing at all. Include terms that:

- state when payment is due
- set a default interest rate for late payment, and
- provide for recovery of full legal costs, should you have to take enforcement action.

If appropriate, include specific reference to creating a security interest pursuant to the Personal Properties Securities Act 1999. This will enable you to become a secured creditor. If you do this, you will also need to be aware of the process for registering a financing statement on the Personal Properties Securities Register at www.ppsr.govt.nz/cms, without which your security won't be complete and is likely to be ineffective.

Take steps as soon as a customer is late. Speak with them if possible. If not, write to them. Too often debtors are not contacted early enough and a problem that could have been a minor one becomes a major one.

The overall key is to take care with your procedures and documentation at the outset of the transactions. It may require time and money to put everything in place but it will more than pay for itself over time.

Lawyers often deal with creditors who fail to recover some or all of their debt, despite having provided an excellent product or service, because they haven't taken enough care or obtained adequate advice when setting up their paperwork and procedures.

New disclosure obligations for Investment Advisers and Brokers

Over the past six months, many finance companies have either failed completely or run into trouble. So it should be comforting to know that the Government has indicated a willingness to legislate to protect the public by passing into law the Securities Markets (Investment Advisers and Brokers) Regulations 2007 (the "Regulations").

The Regulations supplement and update the Securities Markets Amendment Act 2006. Commencement Order SR 2007/367 provided for the Amendment Act to come into force on 29 February 2008, the same day as the Regulations. They are now either contained in or read together with the Securities Markets Act 1988 ("the Act").

Intention of the changes

The intention of the amendments and regulations is to oblige Investment Advisers and Brokers to make certain disclosures to clients in a prescribed manner before giving investment advice or providing services as an Investment Adviser or Broker.

What must be disclosed?

An Investment Adviser must disclose in writing, in the manner prescribed, the following:

- experience and qualifications
- criminal convictions and adverse findings in any Court on their professional role
- the nature and level of any fees charged
- details of remuneration or awards they received or will receive from anyone else
- other interests and relationships that could affect the advice
- types of securities they advise on

It is important to note that clients do not have to ask for this information; it must be provided up-front.

Who is an Investment Adviser or Broker?

An Investment Adviser gives recommendations, opinions or guidance relating to investment in securities to members of the public in the course of the adviser's business or employment. Certain information will not constitute advice, such as opinions published in the media, assistance with acquiring and disposing of securities, and offer documents including a registered prospectus and authorised advertisements.

An Investment Broker receives investment money or property from members of the public in the ordinary course of their business. Therefore, the definition of an Investment Adviser or Broker can include share brokers, financial planners, accountants, lawyers and others that give investment advice to the public.

One point that will be of real interest is the requirement for Investment Advisers and Brokers to disclose their commission structure and the amounts before advice is given. That includes all remuneration whether direct or indirect, that the Adviser or Broker may receive following the giving of advice.

Criticisms

The regulations have been criticised for not going far enough as 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. Furthermore, the regulations do not provide for a declaration of any conflict of interest and a consequent prohibition if a conflict does arise.

It has been suggested that a client agreement should be introduced that clearly sets out the risk associated with the investment being considered. It has also been argued that because a person's life savings may be at stake, the Government should consider passing more comprehensive laws requiring Advisers to fully apprise unsuspecting investors of the risks being taken and make it part of the Investment Adviser's job to assess the client's situation and make a recommendation based on that. Legislation aimed at ensuring that the risk is understood could be the next step.

Remedies

An Investment Adviser or Broker who fails to disclose in accordance with the Act commits an offence, and may be liable for a maximum fine of $100,000 for an individual and $300,000 for a body corporate. However, the Investment Adviser or Broker has a potential defence if he or she believed on reasonable grounds that the disclosure given was not deceptive, misleading, or confusing.

It is hoped that these changes go some way towards increasing transparency and reducing the types of losses we have seen recently.

Enduring powers of attorney – Significant changes

Enduring Powers of Attorney involve an individual, 'the donor', placing trust in a person, 'the attorney', to act competently in the donor's best interests. The donor of such a power who becomes mentally incapable is dependent on some other trusted person to make decisions for him or her. Sadly, this trust is sometimes abused, particularly by family members.

The Government realises the current legislation is inadequate and has enacted the Protection of Personal and Property Rights Amendment Act 2007 ("the Act"). The Act arises out of the Law Commission Paper "Misuse of Enduring Powers of Attorney", received Royal Assent last year and comes into force on 26 September 2008.

The Act makes the interests of the donor paramount. Where the donor has lost capacity, and decision making is taken over by an attorney, the donor still has the right to be consulted about their views. The Act places an obligation on the attorney to encourage the donor to develop the donor's competence to manage his or her own affairs in relation to his or her property.

New witnessing requirements

The Act introduces new witnessing requirements for all new Enduring Powers of Attorney. A lawyer, legal executive, or an officer of a Trustee Corporation must act as the witness. Legal executives are able to witness if they have at least 12 months experience, hold a current annual registration certificate issued by the New Zealand Institute of Legal Executives, and are employed by and under the direction and supervision of a lawyer.

The witness must explain to the donor the effects and implications of the Enduring Power of Attorney and his or her rights, and certify in the prescribed form that this has been done.

At the time of signing, the witness must certify that he or she has no reason to believe that the donor lacks mental capacity and that the witness is independent of the attorney.

New definition of mental capacity

A donor is deemed mentally incapable if he or she lacks the capacity to:

- make a decision about a matter relating to personal care and welfare
- to understand the nature of decisions about matters relating to his or her personal care and welfare
- to foresee the consequences of decisions about matters relating to his or her personal care and welfare, or
- communicate decisions about matters relating to his or her personal care and welfare.

A prescribed form has been issued for Health Practitioners to certify as to incapacity. The form must be used on all occasions when the donor's capacity is in question.

Proper Records to be kept

The attorney must keep proper records of each financial transaction entered into by the attorney while the donor is mentally incapable.

Suspension

The Act allows the donor who has been, but is no longer, mentally incapable to suspend the attorney's authority to act by giving written notice to the attorney. The suspension does not revoke the Enduring Power of Attorney and can be reviewed by a Court. However, an attorney whose authority is suspended cannot act unless a Health Practitioner has certified, or the Court has determined, that the donor is mentally incapable.

Easier access to Courts

A wider range of people can now apply to the Court regarding an attorney's actions. Any of the following people may apply to the Court to review a decision:

- the donor
- a relative or attorney of the donor
- a social worker
- a medical practitioner
- a trustee corporation
- the principal manager of any place that provides hospital care, rest home care or residential disability care
- any welfare guardian who has been appointed for the donor
- a person authorised by a body or organisation contracted by the Government to provide Elder Abuse and Neglect Prevention Services
- any other person, with leave of the Court

In conclusion

It is hoped the Act goes some way to limiting situations in which it might be possible for Enduring Powers of Attorney to be misused or abused. Although compliance costs will inevitably be increased, this is considered a small price to pay to increase protection for a vulnerable donor.

Farm succession – Planning ahead

The most important decisions pertaining to the family farm are made when the boots are off and the kettle is on. There are many difficult questions that must be discussed and resolved by the farming family, including how to achieve the most tax effective outcome while reflecting an ownership structure that meets the needs of the farming family now and in the future.

Farm succession differs from non-farm based estate planning in that the farm is the major asset. As such it needs to provide retirement income for the retiring generation, as well as employment and income for the younger generation.

Elements of a good succession plan

The starting point of any succession plan is to consider what the goals and aspirations are for each member of the family. These will include business, personal and financial goals.

In planning for these goals you will need to consider the following issues:

- the possibility of keeping the farm in the family
- what age the older generation wish to retire – are they going to wind down slowly on the farm or retire to another property
- the desired level of retirement income
- is the younger generation ready to succeed and do they have the skills and commitment to run a farming business
- will the younger generation take on an acceptable debt burden and how will they pay out the other siblings
- fairness to non-successor siblings
- business structures – whether it will be a trading/family trust, sole trader, partnership, a limited liability company or a combination of two or more of these
- tax implications for all of the above
- the distinction between the farm operating as a business and the ownership of farm assets

Implementing the plan

Once the family goals have been developed and outcomes agreed, the next step is to seek professional advice regarding business structures and tax implications. Your lawyer and accountant should work closely together to discuss options with you in order to implement the best structure to enable your family to achieve their goals. The long term benefits achieved by restructuring correctly outweigh the short-term associated costs.

It is prudent to start early as it may take some time to put the structure in place and to transfer assets. The final structure must be able to adapt to changing needs.

Plan maintenance

Ensure the plan is revisited regularly, especially when there are new additions to the family, marriages or de facto relationships, or deaths. Make sure all family members have an up-to-date will. Enduring powers of attorney are also important to have in place, of which there are two types, a 'property attorney' and a 'personal care and welfare attorney'. In both cases these are people who you trust to make decisions and act for you when you are unable to make decisions for yourself.

Throughout the whole process remember the key to success is careful, well informed consideration of all the issues, and effective and early communication with each other and your advisers.

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