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23/6/17

Submission of the Ross Asset Management Investors Group (RAMIG) in response to Report No 2 of the IWG on voidable transactions, Ponzi schemes and other corporate insolvency matters.

We write to you on behalf of the Ross Asset Management Investors Group which represents about 450 investors who were caught up in the Ponzi run by David Ross.

We attach our original submission to the review, 'Brief for Insolvency Review 20160222' which forms part of this submission.

We are grateful that the second report of the IWG was released recently, particularly covering Ponzi aspects. However, we have concerns about the effectiveness of the document.

It is now apparent that recoveries from the RAM Ponzi will be unacceptably bad, with less than one third of the stolen money now available for recovery by the liquidator. We expect only a fraction of this third to ever be recovered, once costs and other factors are considered.

The remaining two thirds of the stolen money is locked out of the recovery process and cannot now be recovered in any way. We are now left arguing about the crumbs left under the table before we even start.

The recent decision of the Supreme Court in the Fisk v McIntosh appeal will enable hundreds of RAM investors to benefit from a crime. The Supreme Court has decreed that investors who withdrew their capital prior to the FMA closing David Ross's Ponzi can keep the money even though it was paid out using capital effectively stolen from other investors.

By enabling investors in a criminal activity to benefit from the crime the Supreme Court (or the law) has deviated from the principles upon which our justice system is based.

This is an unacceptably unfair outcome and a blight on the NZ financial markets. The issue must be addressed effectively and urgently by government, if investor confidence is ever to be restored to the levels it should be in this country.

The report is described in your media release as the second and final report of the IWG.

The report has a vital role of informing the lay public of the issues so that they can comment and make meaningful submissions.

The report makes very limited suggestions with respect to Ponzi's, in a form that is incomprehensible to most of the public. We surmise only a few elite practitioners involved in the field will be able to fully understand the issues raised. The IWG appears to have no one on it representing investors (especially small investors), and we believe this shows all too much in their output.

The recommendation of a 'reasonable investor' test is necessary, but most readers will not understand the implications of such a suggestion from what is written in the report, especially as they apply to RAM. Such a vague concept as a 'reasonable investor' test may need years before the courts before we understand what it actually represents, or if it might solve some of the problems raised by RAM.

Similarly, the recommendation of a compensation scheme is necessary, but the description is so fleeting as to be almost trivial. Most of the comments about the compensation scheme in the report are negative. Issues such as how to fund the proposed scheme do not seem to be covered. An investors compensations scheme of some sort is desperately needed without other effective measures to stabilise the environment for small investors.

The report acknowledges the need to keep regular statistics on insolvencies, but the statistics must focus on reporting on the effectiveness of the insolvency industry.

The report does not consider that as a crime has taken place, some of the recovery burden should be carried by the state, as it would be with other crimes. Alternatively, or in addition, the minority of investors who have made disproportionate gains relative to other investors from the RAM Ponzi should bear more of the recovery burden or forgo a proportion of the distributions.

The second report does not seem to cover the issues of what constitutes a fair and just outcome, and does not seem to cover the issues of letting investors keep money stolen from other investors.

The solution must be investigated, that in the case of a Ponzi, all stolen funds should be recovered and then distributed rateably to all investors so that investors are all equally disadvantaged.

It is such issues of fairness that most of the public relate to, and we are sure that the minister will be well in tune with such public sentiments, and the need to discuss them openly in a review like this.

With submissions on the second report closing on 23rd June it seems impractical with the information provided for the public to make meaningful submissions.

The report is essentially incomprehensible to ordinary people and it does not seem to answer basic questions the public have about a fair and just outcome.

Yours sincerely,

for RAMIG

Ross Asset Management Investors Group (RAMIG)

Brief for Insolvency Review – 20160222

Executive Summary

The Minister of Commerce and Consumer Affairs has announced a review of the insolvency laws in NZ, including the law relating to unwinding Ponzi schemes, such as Ross Asset Management. (See http://www.beehive.govt.nz/release/expert-group-set-review-insolvency-law).

The Ross Asset Management investors group applauds this review so long as it takes a holistic view and properly addresses the profound problems of the insolvency industry in their entirety.

Because of the apparent absence of an investor perspective in the makeup of the review team, RAMIG has prepared this investor focused brief, offering an emphasis on the detrimental impact of crime, recklessness and incompetence in the investment markets, including a specific focus on Ponzi related frauds.

The fact that the RAM receivership/liquidation has taken 3 years and cost the investors approximately $2 million dollars 'so far' in fees to arrive at the current point is undeniable proof that current laws and processes are grossly inadequate. The victims of the RAM fraud still don't know what part of the $115 million stolen by RAM will be returned to its rightful owners.

The unacceptable pattern of poor recoveries, uncertainty, high costs and long delays seems to have been all too common with the large number of insolvencies and Ponzi's in NZ in recent years. The effect has been to destroy confidence in the financial markets and expose investors, many of them elderly, to such immense stress that most are forced to simply give up as a way to survive emotionally.

Insolvency law must create an effective ambulance at the bottom of the cliff for investors, and must blend with protection (fences) at the top of the cliff (such as the Financial Markets Conduct Act or FMCA) to provide better overall protection and recovery for investors, especially in major collapses in the financial markets which now occur frequently. Could recoveries for investors have been much better after the Global Financial Crisis (GFC) if NZ had had better insolvency law in place? Are investors exposed to excessive and increased risk by our current insolvency law?

It appears there are profound issues in our insolvency laws that may effectively destroy property rights, people's ownership of their funds and prevent equitable outcomes.

Current laws and processes seem to be chaotic, out of balance and provide the means whereby those who have benefitted from crime seem too often to be able to keep their gains at the expense of those who lost, notwithstanding incidents where the beneficiaries were unaware that a crime had taken place.

It appears that insolvency/recovery environments in other countries are superior to NZ. For instance investors in the US Madoff Ponzi are told by their liquidator to expect high rates of recovery. We must ask why NZ investors have been left so exposed for the past 50 years, whereas investors in other countries have been offered far better protection.

The review must analyse and report on the following issues:

BRIEF

1. The review must seek to restore confidence in NZ's financial markets. Confidence has taken a battering because of the billions of dollars investors have lost due to crime, recklessness and incompetence, especially since the Global Financial Crisis of 2008. It seems the NZ legal environment has encouraged a culture of recklessness and fraud in the financial markets.
2. The review must have an investor focus, especially towards small investors.
3. The review must balance protection with acceptance of reasonable risk for investors, and avoidance of unreasonable moral hazard issues.
4. The review must provide clear and objective outcomes that provide a clear path and can be readily understood, especially by investors. Review outcomes that are vague, subjective, and excessively legalistic, that rely on concepts that will need to be resolved in future in court, or do not address the issues; will not restore investor confidence in NZ's financial markets. Is Ponzi specific legislation required?
5. The review must identify other investment vehicles which are widely used currently in NZ and have the same vulnerabilities as RAM. For instance where the investors name does not appear on the title of equities, and hence issues such as ownership of investor funds arise. RAMIG believes such exposures are currently massive for NZ investors across a wide range of NZ investment vehicles, besides RAM.
6. The review must set benchmarks to measure the performance of the insolvency industry, such as the amounts initially lost/recovered by investors, the costs of recovery, the times of recovery. It seems the current performance of the insolvency industry cannot be said to be adequate, in fact it could be said to be dysfunctional. The recent past must be compared with the future performance to ensure the industry is doing better.
   A source list of collapses and insolvencies can be viewed at http://www.interest.co.nz/saving/deep-freeze-list but further work is needed on this information to complete the fields listed above.
   The losses are not only a cost to victims of fraud but to the total population as it ties up the court system for years instead of a few weeks or months.
   If we are not measuring the performance of the insolvency industry how can we claim we are managing the industry, or if it is doing better or worse for investors?
7. The review must be seen to balance the interests of all parties. Currently the long delays, complexity and vagueness seem to favour winners and liquidators, at the cost of losers who have done very badly of late. Recovery is currently a massive lottery that most often goes on for years. NZ's ill-fitting insolvency law creates massive uncertainty, cost and delay.
8. Ownership of investor funds. In the case of a Ponzi the money is stolen from investors so it should never become the property of the company. Who is entitled to uplift the money on behalf of the investors and restore it to the rightful investors, without diminishing the investor's property rights? Where is the 'value-add' in destroying or diminishing the 'property value' of investor's money? Note: that a painting that is stolen can be recovered years later by its rightful owner, even if on sold to a third party. Why is money treated differently from other property, how does this 'add value' for investors?
9. The review must settle what is a fair and just manner to unwind a Ponzi scheme. Should all investors be equally disadvantaged by requiring all funds to be placed into a pool and the

funds returned in proportion to the amount invested (adjusted for the variation in effective value over time). In unwinding a 'perfect' lossless Ponzi all investors would end up with their original capital, though it is accepted this is unlikely in practice. The current system with its tests which do not seem to relate to fairness and its low rate of recovery effectively leaves the fraudster to redistribute most of the investor' wealth, and opens the whole investment environment to increased opportunities for corruption. It is not acceptable to simply leave the money where it fell (or was placed by a fraudster or reckless person) once the fraud is discovered.

Is a fair and just recovery better served by tests that are based on the principles of equity? How are claims for the same money to be handled if equity claims compete with claims under the Companies Act or Property Law Act?

10. Are prison sentences for fraudsters adequate? Are the current short prison terms more of an incentive than a deterrent? The current low level of sentences are an affront to many investors who have been robbed. White collar criminals seem to have a specially privileged position in our society; this perception impacts investor confidence.
11. Should fraudsters be able to negotiate lower sentences if they cooperate constructively, eg by identifying those who had knowledge of what was going on before the collapse.
12. Should there be standard prison terms or penalties for the amounts stolen – eg one year in jail for each $ million stolen? Sentences are currently grossly mismatched in terms of years in jail versus the amounts stolen (eg David Ross got one day in jail for each approx. $60,000 stolen, another gets one day in jail for each approx $100 stolen). Such disparities create perverse incentives for fraudsters and encourage reckless advisers/traders.
13. It appears some fraudsters and close relatives are able to retain high levels of visible assets (eg homes worth millions of dollars) even after they have been shown to defraud investors of hundreds of millions of dollars. These high levels of retained assets should be measured and comments made whether this situation is satisfactory or not?
14. What reparations are being provided by fraudsters, what is a reasonable level?
15. How can group claims (class actions, or sharing of common lawyers) be enabled to prevent investors from having to take individual claims to court? The high complexity, cost and risk of individual actions is denying justice to investors, especially small investors. Conversely, the pressure is apparent for net winners in the RAM Ponzi who wish to defend their gains, potentially individually.
16. The cost of pursuing claims against debtors to recover money in insolvency cases seem to be so complex, uncertain and expensive that often very few claims can be progressed economically, leaving very low recovery rates for investors who have lost money. Further, the need to trace individual transactions, sometimes at huge cost per transaction, often makes the cost of recovery prohibitive. How can such log jams be removed or improved? Are there ways to tag and track investor's funds (especially using modern technology) to enable title to be protected; is there any work or progress in this area globally?
17. Are the tests (and voidable transaction/claw back periods) under the Companies Act and the Property Law Act appropriate to produce fair and just outcomes when recovering stolen funds? Given the unsatisfactory recent outcomes, especially with Ponzi's, it seems not. Are the tests such as 'acted in good faith', and 'didn't have knowledge of insolvency' and; 'gave value' or 'altered position' the best tests? These tests don't seem to relate to fairness and justice (equity) or otherwise set reasonable expectations for levels of recovery.

The 'had knowledge' test simply conditions the market behaviour of the informed net winner, who knows to pretend they didn't know. Any 'good' legal advice to the net winner will ensure this. After the fraud is discovered everyone has the knowledge, so why should different rules apply before and after?

Giving value seems have become a farce, exampe one RAM net winner investor has been allowed by the High Court to retain his initial capital invested in the RAM Ponzi (even though it is stolen from other investors), yet other net loser investors are apparently not deemed to have given value (currently subject to appeal).

The change of position defence needs to be clarified to let small and innocent net winners have reason to expect they are reasonably protected from claw back – e.g. the net winner widow or retired couple who has taken only reasonable living expenses over the period of the fraud.

Repeating from above, is a test based on equity more appropriate?

18. Claw back periods need to be reassessed to ensure fair and just outcomes are possible. Is the apparent 3 year claw back that has been unilaterally set by the liquidator in the case of the RAM Ponzi reasonable? Is the imposition of such a limit simply a reflection of the weak insolvency recovery environment? How does the Limitations Act impact the amount that can be recovered, and are its setting correct for these situations?
19. The issues of fidelity funds and insurance to protect small and vulnerable investors (in line with the say USA SIPA 1970) need to be thoroughly investigated and amendments to current NZ law suggested. The current idea that investors have to foot the cost of recovery and the finance industry is allowed seemingly to walk away from the messes that it has created or allowed to be created, needs to be thoroughly reported.

    Such a fund would act as a deterrent to would be fraudsters, knowing that other market operators would most likely dob them in (to save themselves cost) if they had the slightest suspicion. Currently this is little such incentive; the industry is not set up to be effectively self-policing. Evidence of widespread knowledge and corruption seems to have not been adequately investigated.
20. It seems impossible or too hard to perform a comprehensive retrospective forensic analysis of the actions of many of NZ's fraudsters. This certainly means huge sums of money that rightfully belongs to investors have disappeared. The law must recognise that crooked or reckless financiers have huge opportunities to hid money for their own benefit, especially offshore. Better up front audit procedures should make retrospective forensic analysis easier.
21. Current law seems to set the liquidator/receiver up as an independent contractor acting on behalf of investors. Does this set up incentives for the liquidator/receiver to maximise his own position before that of the investors? This may explain the high liquidator/receiver costs/fees compared to investor recoveries in many cases. Another negative to this process is that when liquidators/receivers fees have exhausted the liquidated assets they have also exhausted the chance of a just outcome. This supports the view that a fidelity fund should be mandatory in the financial markets.
22. The responsibilities of institutions such as banks to detect fraud and provide more protection for investors needs to be investigated and reported. The responsibility of the State to detect and investigate problems needs to be clarified, especially the roles of the FMA and SFO. Is the process for taking claims against advisers viable, does this avenue offer

potential returns that equal the amounts lost? Based on the scale of the amounts lost this does not seem to be the case.

23. Retrospective legislation to provide a fair and just outcome for the investors of frauds that have already been detected (such as RAM investors) needs to be analysed and reported.
24. Have investors in many earlier Ponzi's and frauds simply been ignored in the past and the problems swept under the carpet because of inadequate insolvency law?
25. Have the pickings just been too good for fraudsters and reckless traders, has NZ really tackled corporate corruption in the past and is this review going to do something substantive about it?
26. The proceedings of unravelling white collar crime are often kept highly secret from investors by liquidators/receivers? Should liquidators/receivers be required to make their proceedings more open and transparent to investors?
27. Any new regime for liquidators/receivers arising from this review must not create additional inappropriate advantage, monopolies, or opportunities for endless litigation for liquidators/receivers/lawyers and work against the interests of investors.