MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
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COVERSHEET

Minister	Hon Kris Faafoi	**Portfolio**	Commerce and Consumer Affairs
Title of Cabinet paper	**Insolvency Law Reform**	**Date to be published**	4 November 2019

List of documents that have been proactively released		
Date	**Title**	**Author**
23 September 2019	*Insolvency Law Reform*	*Office of the Minister of Commerce and Consumer Affairs*
23 September 2019	*Insolvency Law Reform: Annex One - Minor Changes*	*Office of the Minister of Commerce and Consumer Affairs*
23 September 2019	*CAB-19-MIN-0491*	*Cabinet Office*
23 September 2019	*Regulatory Impact Statement: Insolvency Law Reform – Gift Cards & Vouchers*	*Ministry of Business, Innovation and Employment*
23 September 2019	*Regulatory Impact Statement: Insolvency Law Reform – Reckless Trading Claims*	*Ministry of Business, Innovation and Employment*
23 September 2019	*Regulatory Impact Statement: Insolvency Law Reform - Voidable Transactions*	*Ministry of Business, Innovation and Employment*

Information redacted **YES**

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Some information has been withheld to maintain the constitutional conventions for the time being which protect the confidentiality of advice tendered by Ministers of the Crown and officials.

Impact Summary: Gift cards and vouchers

Section 1: General information

Purpose
The Ministry of Business, Innovation and Employment is solely responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing final decisions to proceed with policy change to be taken by Cabinet.

Key Limitations or Constraints on Analysis

The objective of this document is to provide analysis on options to deal with claims in respect of amounts owing on unused gift cards and vouchers when the company that issued them is placed into liquidation.

The Insolvency Working group (**IWG**) was formed in 2015 as part of the Government's review of corporate insolvency law. It comprised an independent chair, two insolvency practitioners, two insolvency law specialists, a credit industry expert and a representative of the Official Assignee.

The issue covered in this RIA relates to the uncertainty that holders of unused gift cards and vouchers face when the company issued them went into liquidation. It was identified by the IWG in the second of its two reports (**Report No. 2**).

Lack of aggregate data on significance of gift card debt to a company's outstanding debt
A main assumption in our analysis is that gift card and voucher value is typically a small proportion of a company's outstanding debt (less than 10 percent), therefore liquidators' treatment of gift card and vouchers will not impact on their decisions about whether the company could continue trading or close the business immediately. This means that decisions around gift cards are unlikely to materially compromise on the *pari passu* (equal sharing) principle that underpins insolvency law, i.e. the collective interests of all creditors.

This assumption is based on our initial discussions with insolvency practioners. We have sought, but not yet received, data from individual cases. There are also limited cases of liquidation where gift cards and vouchers data were collected and available.

Arbitrary decision on the level of value that should be honoured
One of three options that were assessed was to require businesses to honour 50 percent of gift cards and vouchers' value if they continue to trade after insolvency or administration commences. The decision to set the level at 50 percent is inevitably arbitrary. It's largely based on the need to minimise the impact honouring gift cards will have on the cash flow of businesses, and the decisions of insolvency practitioners about whether to continue trading or close a business immediately.
Range of options considered

The three options considered in the RIS include the IWG's proposal, the status quo and an alterative option. The option of the dollar-to-dollar matching approach that is adopted

by some insolvency practioners (i.e. honouring up to 50 percent of value as long as the consumer also spends the equivalent amount) has not been included, because it would exclude low income consumers who could not afford to match the value of the card or voucher.
Responsible Manager (signature and date):
Susan Hall, Manager, Corporate Governance and Intellectual Property Policy, Commerce, Consumers and Communications Branch, Building, Resources and Markets Group, Ministry of Business, Innovation and Employment

Section 2: Problem definition and objectives

2.1 What is the policy problem or opportunity?

The primary problem:

This is a consumer protection issue that comes to prominence from time-to-time, particularly when a major retail chain enters administration or is placed in receivership or liquidation. Gift card and voucher holders are ordinary unsecured creditors, which often mean that they will receive nothing in the event of company insolvency.

Why is it important to address:

Receivers and liquidators are not required to honour gift cards and vouchers when they decide that the business will continue to trade. Nevertheless, some insolvency practioners choose to honour up to 50 percent of the value as long as the consumer also spends the equivalent amount. But there are various other practices.

This raises consumer protection issues because unlike most other classes of creditors, recipients of gift cards and vouchers cannot be expected to monitor the solvency of retailers or know that a retailer will not be required to honour a gift card or voucher should they become insolvent at a later date.

Cause of the problem:

Gift cards and vouchers are essentially a form of prepayment, to be used as an alternative to cash for purchases within a particular store or related businesses. If a customer is left holding a gift card or voucher issued by a company in liquidation, there is no certainty that the gift card or voucher will be honoured by the liquidator of the company. Liquidators may, but are not obliged to, honour gift cards/vouchers.

Why now:

The Insolvency Working Group (IWG) was established to review corporate insolvency law and provide advice to the Government on areas of reform. One of the IWG's proposals was related to preferential claims, where amongst other things, the IWG recommended establishing a new preference for gift cards and vouchers, ranking equally with the layby sales preference.

MBIE does not think IWG's proposal would be workable, mainly because it would incur disproportionally high administration costs for liquidators and receivers. These costs would be a drain on the finite pool of assets available to other creditors. It will also do little to promote consumer protection as consumers would need to register their claims in order to be eligible to receive anything, and there would be considerable delay before consumers would be paid.

MBIE's preference was to retain the status quo. However it was asked to provide alternative options. The alternative, which is the preferred option, has been included in this analysis.

The objective outcome:

The objective is to find a solution that can provide some protection to consumers without materially impacting the collective interests of ordinary unsecured creditors.

MBIE proposes an alternative approach to creating a preference, which will overcome the need for liquidators and receivers to undertake an extensive administrative exercise, yet provide certainty to gift cards and voucher holders.

2.2 Who is affected and how?

MBIE's position is that no changes should be made to the insolvency law. MBIE was asked by the Minister to provide alternative options instead of retaining the status quo. As a result, MBIE proposes the law be amended to require businesses to honour at least 50 percent of the value of gift cards and vouchers if they continue to trade after a formal insolvency administration or liquidation commences.

The proposal will impact on

- *gift cards and vouchers holders*. These parties will have the certainty that they are able to get at least 50 percent of the value of any unused gift cards or vouchers if the business continues to trade (note that some liquidators already do this, subject to the consumer spending an equivalent amount). This will make consumers no worse off and, often better off, in comparison with the status quo.

- *businesses that issued gift cards and vouchers that continue to trade after liquidation*. Instead of leaving claims by gift card and voucher holders to the discretion of liquidators, businesses will be required to honour at least 50 percent of the gift card/voucher value. Anecdotal evidence suggest that being required to honour 50 percent of outstanding gift card value is unlikely to affect insolvency practioners' decisions about whether to continue to trade or not after the company enters formal insolvency proceedings. It is also possible that honouring at least 50 percent of gift card/voucher value would lead to extra sales for the company.

- *Liquidators and receivers.* It will not have a significant impact on liquidators and receivers compared with the status quo. However, this proposal will be considerably better for the liquidators and receivers establishing a priority because they will not need to incur potential significant administrative costs to deal with their claims.

- *Other unsecured creditors*. Other unsecured creditors should not be materially impacted by this proposal. While the collective amount available for re-distribution might reduce slightly due to businesses having to honour 50 percent of gift cards, the amount involved in connection with gift cards and vouchers is usually only a small proportion of the total debt owed to all creditors (under 10 percent). It is therefore unlikely to materially harm the interests of other creditors. While we do not have aggregate data, we expect that the reduction in liquidators' fees from not having to deal with claims from gift card holders should offset, to a great extent, the reduction of total amounts available for re-distribution to unsecured creditors.

2.3 Are there any constraints on the scope for decision making?

MBIE's preference is the status quo, i.e. rejecting the IWG recommendation and making no change to the current status of gift cards and voucher holders. The Minister has asked MBIE to provide alternative options to addressing the issue around gift card and voucher holders in a retailer's collapse.

The status quo has been included in our assessment of the range of options, both as it serves as a yard stick for comparing other options and for transparency reasons.

Section 3: Options identification

3.1 What options have been considered?
The three options that have been considered are: 1. MBIE's original proposal to make no change to the current status of gift cards and vouchers. 2. Alternative MBIE proposal to require businesses to honour at least 50 percent of gift card and voucher value, if they continue to trade after insolvency or administration has commenced. 3. IWG's recommendation to establish a new preferential claim for gift cards and vouchers, with the same ranking as layby sales. We assess the options against the following three objectives: **A. Consistent with the equal sharing principle** This objective will be achieved if all unsecured creditors are ranked equally and are paid the same dividend in insolvency. **B. Consumer protection** It is inevitable that a business in receivership or liquidation won't have enough available assets for all its creditors. This objective will be achieved if gift card and voucher holders would have more protection than currently – either via being guaranteed to be prioritised for distribution, or having more certainty of how much they would likely to get, or both. **C. Administrative efficiency** This is achieved when the following costs are minimised as far as possible: • costs associated with the processes for a liquidator to take possession of, protect and realise, and distribute the assets of the company to its creditors, and • compliance costs for creditors against whom claims are made.

3.2 Which of these options is the proposed approach?

Given the status quo is out of scope, MBIE recommends option 2, because it:

- minimises the administration costs that would otherwise be associated with processing claims from gift card and voucher holders,
- will not benefit one group at the expense of other creditors, and
- still offers a reasonable level of consumer protection for these creditors.

Option 1: status quo	Option 2: honour at least 50 percent of value (alternative option)	Option 3: new preferential class (the IWG)
Equal sharing		
Wholly consistent the equal sharing principle	Weakens the equal sharing principle, but not to the same extent as option 3, given only 50 percent of value will be honoured, and only when business continues to trade. Limited impact on unsecured creditors as gift cards holders will only be entitled to half of the value of their gift cards/vouchers ahead of other unsecured creditors (some liquidators already do this but in an ad hoc way).	Weakens the equal sharing principle as there are other forms of prepayments that do not have preferential status Reduces the remaining pool of assets available for redistribution to all unsecured creditors
Consumer protection		
Less supportive of the consumer protection compared to the other two options, as treatment of gift cards/voucher holders are left to discretion of liquidator/receiver.	Benefits low income consumers who do not have the discretionary income to satisfy the dollar-for-dollar approach that liquidators sometimes adopt. But no benefits if stores close immediately. Voucher holders have certainty of getting at least 50 percent of voucher value, and do not have to go through claim process with liquidators.	Only supports a selected group of consumers (those with unused gift cards/vouchers). The extent of protection for them is also relatively insignificant, given that the most common value of gift cards being $50-$70. This option will also have a negative impact on other consumers such as IRD.
Administrative efficiency		
Administratively efficient as liquidators/receivers determine the most appropriate approach	Administratively efficient as liquidators or receivers will not need to separately process claims from gift card holders, and gift card holders do not incur costs by having to submit claims.	Not administratively efficient. Adding another preferential class will substantially increase liquidators' fees to deal with disproportionately insignificant claims. In many cases the additional administrative costs will exceed the value of the gift cards. or vouchers

Section 4: Impact Analysis (Proposed approach)

4.1 Summary table of costs and benefits

Affected parties *(identify)*	**Comment**: nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks	**Impact** *$m present value, for monetised impacts; high, medium or low for non-monetised impacts*
Additional costs of proposed approach, compared to taking no action		
Regulated parties	Businesses that continue to trade need to honour at least 50 percent of voucher/gift card. Holders of gift cards and vouchers will lose up to 50% of voucher/gift card value but have more certainty, and are better off because in other cases they might not get anything	Minimum impact as gift cards typically are of small monetary values, and are of minor proportion of a business' outstanding debt Lose 50 percent of the gift card/voucher value if the business continues to trade. Given typically small value (around $50-70), negative impact is low
Regulators	n/a	n/a
Wider government	n/a	n/a
Other parties	Other unsecured creditors will not be materially worse off because 50% of gift cards and vouchers will only be a small proportion of debtor's debt	No cost on liquidators Low cost on other creditors
Total Monetised Cost	-	-
Non-monetised costs		***Low***

Expected benefits of proposed approach, compared to taking no action		
Regulated parties	Businesses will be required to honour at least 50 percent of gift card value, instead of potentially pay 100 percent. Gift card and voucher holders will have certainty that they could receive at least 50 percent of value if business continues to trade	Low as gift card values are typically an insignificant proportion of outstanding debt. Might also get extra business as a result. Low. Gift card values are typically very low value so the benefits are unlikely to be significant.
Regulators	n/a	n/a
Wider government	n/a	n/a
Other parties	n/a	n/a

Total Monetised Benefit		
Non-monetised benefits		***Low***

4.2 What other impacts is this approach likely to have?
Gift card and voucher holders would receive no additional benefit if stores are closed immediately. Those consumers that are in some parts of the country may also find it difficult to take advantage of the policy if the stores in their region close but others remain open. However, this would be less of an issue if online trading remains available. There is a possibility that gift card and voucher holders would suffer a greater proportional loss than other creditors of the business, if the rate of recovery for other creditors were higher. There could be negative impacts on creating some inequality for creditors with other forms of prepayment (e.g. those that pay under instalment plans and deposits) that are not able to get certainty of how much they could claim back. There is also a risk of schemes being designed to get around a legal definition that is focused only on gift cards and vouchers. However, we do not consider this is a significant risk as we think it unlikely that trading business would restructure their affairs in this way in anticipation of insolvency.

Section 5: Stakeholder views

5.1 What do stakeholders think about the problem and the proposed solution?
The IWG's report No. 2 was publicly consulted in 2017. Eleven submitters commented on IWG's recommendation to establish a new preferential class for gift card and voucher holders. Consumer NZ supported IWG's recommendation. They noted that recent high profile retailer insolvencies have left gift card holders out of pocket, and given gift cards' popularity with consumers, it would help protect this class of consumers if they have the same protection as layby customers. Kengsington Swan supported the recommendation. PWC also agreed, but noted that it would result in other types of prepayments were treated differently. Simpson Grierson was not object to the proposal, but noted a number of practical issues that would need further consideration (e.g. better definition of scope, and counterparty, giving receivers means regarding prescribed notice procedure and cut-off date, and whether there should be an expiry date). Most submitters (individual, KordaMentha, Grant Thorndon, Bell Gully, EY, McGrath Nicole, CPA Australia, Russell McVeagh) were against the IWG recommendation mainly due to the administrative burdens involved and how disproportionate it would be to the value of gift cards. Bell Gully also highlighted that gift card holders were not similar to layby customers and should not be treated similarly. Some noted that they did not think it was equitable to

prefer one type of pre-payment over another form, and honouring gift cards might not be in the interests of creditors, esp. when gift card claims were greater than the value of stock on hand. Similarly, RIATNZ (Restructuring Insolvency and Turnaround Association of NZ) noted that the unreliable record retailers typically kept for gift cards and the low value of gift cards would likely the administrative process time-consuming and expensive.

The alternative option recommended by MBIE (honouring at least 50 percent of gift card/voucher value) was not a subject of public consultation.

Section 6: Implementation and operation

6.1 How will the new arrangements be given effect?
The Companies Act 1993 will be amended to require businesses to honour at least 50 percent of gift card and voucher value, if they continue to trade after insolvency or administration has commenced. We expect to provide instructions to PCO by the end of 2019. It is expected that the new arrangements will come into effect in 2021.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?
We will monitor and review individual cases as and when that happens – i.e. in cases of corporate failures where gift cards are concerned.

7.2 When and how will the new arrangements be reviewed?
We will review the new arrangements from corporate failures where gift cards are concerned, to see how honouring at least 50 percent of gift card/voucher values impact on gift card/voucher holders, insolvency practioners' decisions on whether the business could continue to trade, and other unsecured creditors.