

Submission on discussion document: *A new regime for unravelling Ponzi schemes*

Your name and organisation

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Organisation	Grant Thornton New Zealand

Please select if your submission contains confidential information:

I would like my submission (or specified parts of my submission) to be kept confidential, and attach my reasons for this for consideration by MBIE.

Responses to discussion document questions

1	Are there currently any other methods for resolving a Ponzi scheme which officials should keep in mind? If so, what are they?
	No – As Ponzi Schemes are all very fact specific we favour the current model of letting the Court’s decide the fairness of the distribution method and when done as a directions hearing all sides get to put their case to the Courts.
2	Do you agree with Glazebrook J’s statement that “an accident of timing as to when funds are withdrawn should not favour one defrauded investor over another”?
	We agree with this, but the question is how far do you go back to achieve fairness?
3	Do governing documents ordinarily cover the scenario where an investor is overpaid? If so how is this provided for?
	Do not know, but suspect if there are governing documents they will be silent on over payments.
4	Do you consider that, where investors are all the subjects of fundamentally the same fraud, the strict legal form of a Ponzi scheme should not impact the outcomes of investors?
	Yes.
5	Do you agree with the objectives we have identified for the regime for unwinding Ponzi schemes?
	Yes we agree with the objectives but do not believe a new regime is required to meet the objectives.
6	Do you agree with problems identified with the status quo? Are there any additional issues which we should seek to address?
	No – the discussion document points out that Ponzi schemes are relatively rare in New

	<p>Zealand, we favour the current model of letting the Courts decide the fairness of the distribution method, and when done as a directions hearing all sides get to put their case to the Courts. We feel there is a misunderstanding regarding the cost of distribution process. Our experience is that the major cost is associated with the tracing and managing investments and determining investors' balances. The cost of determining the distribution method is not the biggest cost in our experience</p>
7	<p>Do you agree with the preferred option we have chosen?</p> <p>On balance, we support the option chosen but not the 4-year claw back period.</p>
8	<p>Do you agree with our design goals? Are there any other goals, which the system should be designed to achieve?</p> <p>No.</p>
9	<p>Are there any other factors which you think should be treated as indicating that an investment scheme is a Ponzi scheme?</p> <p>We believe the failure to invest in the promised investments is an important factor.</p>
10	<p>What are your views on our proposed definition of a Ponzi scheme:</p> <ul style="list-style-type: none"> Do you consider that our definition of a Ponzi scheme might capture any investment structures or products which it should not? Do you consider that the definition of a Ponzi scheme should seek to capture any other investment structures or products? <p>We share the concern that any strict definition or list will be used to create new structures designed to fall outside the definition. It is important to ensure there is flexibility for other circumstances and factors be taken into account.</p> <p>We support limiting the definition to the schemes listed</p>
11	<p>Do you consider that the third limb of the proposed definition of a Ponzi scheme should be expanded to capture investments more generally?</p> <p>No.</p>
12	<p>Are you aware of any cases in which our proposed definition would have failed to capture a Ponzi scheme?</p> <p>No</p>
13	<p>Do you agree with the criteria for identifying when an investment scheme should be able to be declared a Ponzi scheme?</p> <p>Yes.</p>
14	<p>Do you consider that there are any additional or alternative criteria which should need to be met in order for a scheme to be declared to be a Ponzi scheme?</p> <p>No.</p>
15	<p>Do you consider that proving fraudulent intent on the part of the operator of an investment</p>

	<p>scheme should be a necessary requirement to establish that that scheme is a Ponzi scheme?</p>
	<p>No.</p>
16	<p>Do you consider that the test for whether an investment scheme is a Ponzi scheme should be:</p> <ul style="list-style-type: none"> • based on a set of fixed criteria? • At the absolute discretion of the courts? • a combination of limited discretion by the courts based on a set of criteria?
	<p>We support this being at the absolute discretion of the courts.</p>
17	<p>Is it appropriate for the liquidator of a Ponzi scheme to have the same duties and powers of the liquidator of a company under the Companies Act?</p>
	<p>Yes.</p>
18	<p>Do you agree that a liquidator should be able to exercise all powers, rights, and privileges that the operator of the Ponzi scheme had prior to that liquidation – notwithstanding that any arrangements contemplate that those powers, rights, and privileges would end on the appointment of a liquidator?</p>
	<p>Yes.</p>
19	<p>Do you think that liquidation is an appropriate model for resolving a Ponzi scheme? If you think a different model is more appropriate, please explain why you consider this to be the case.</p>
	<p>We believe it is an appropriate model.</p>
20	<p>Do you agree that the process for appointing a liquidator is an appropriate model on which to base the process for declaring an investment scheme is a Ponzi scheme?</p>
	<p>Yes.</p>
21	<p>Do you agree that that in order to declare an investment scheme to be a Ponzi scheme the High Court must be satisfied on the balance of probabilities that it is in fact a Ponzi scheme?</p>
	<p>Yes, this seems reasonable.</p>
22	<p>What are your views on the list of parties that would be able to seek a declaration that an investment scheme is a Ponzi scheme?</p>
	<p>The list in para 145 seems acceptable.</p>
23	<p>Do you agree that where the courts consider that a scheme may be a Ponzi scheme, but lack sufficient evidence to make an order to that effect, that the court be able to appoint an insolvency professional to examine the affairs of the scheme?</p>
	<p>We agree with this approach.</p> <p>We recommend that a timescale be placed on the examination, such that a report should be made to the Court on results of the examination within six weeks.</p>

24	What level of certainty that a scheme may be a Ponzi scheme should be required to make such an appointment?
	This should be up to the Judge's discretion
25	How long would it take, and what do you think the cost would be, for an insolvency professional to examine the affairs of a scheme and advise the court whether, in their professional opinion, there is sufficient evidence to conclude that that scheme is in fact a Ponzi scheme?
	This will be fact dependant on each case. Access or availability of books and records may be difficult.
26	Where an investor seeks a declaration that an investment scheme is a Ponzi scheme, should the Crown be required to fund the appointment of the relevant insolvency professional if it is found that the scheme is not a Ponzi scheme? If not who should bear that cost and why?
	No the Crown should not be required to fund it. It should be part of the investor's consideration before applying to have the declaration. An investigation prior to the declaration may avoid/reduce this cost. If the Scheme is found to be a Ponzi then the cost should be borne by the Scheme and not the Investor.
27	Should there be a set period for which an insolvency professional should be able to be appointed?
	We recommend a period of six weeks with ability for the insolvency professional to seek an extension from the court if there are valid reasons to suspect that further relevant information will be available after that period.
28	Do you consider that investment schemes which are invested in only by investment businesses, large persons and government agencies should not be able to be declared to be Ponzi schemes?
	No.
29	Do you consider that it may be in investors' interests for investment schemes, which have invested substantially in a Ponzi scheme, to be able to be wound up as if they were a Ponzi scheme themselves?
	No.
30	Do you think that measures are needed to minimise or mitigate the consequences for an investment scheme or its operator of a failed attempt to have it declared to be a Ponzi scheme?
	We support measures to minimise these risks.
31	Should there be a limit placed on the ability of investors to bring proceedings to have a scheme declared to be a Ponzi Scheme?
	No.
32	Should a defence be available to investors who in good faith bring a proceeding that a scheme is a Ponzi scheme from claims for damages brought by the operator of the

	investment scheme?
	No.
33	Do you consider that there should be a presumption that a Ponzi scheme was a Ponzi scheme for all time (so there is no need to identify when the scheme became a Ponzi scheme unless there is evidence to the contrary)?
	No the scheme may have been operating legitimately at an earlier point in time. We note the difficulties in ascertaining the details of a Ponzi scheme due to lack of records and fraudulent entries may make determining when a scheme became a Ponzi Scheme, therefore such a presumption in these cases may be the best approach.
34	Do you think that there should be a statutory default (say 5 years) for how far back a scheme is a Ponzi scheme in cases where a liquidator is not able to identify a point (or period) at which the scheme became a Ponzi scheme?
	Yes, we believe this should be 2 years so it matches the clawback provisions.
35	Do you agree that, in the case of Ponzi schemes, tracing is an inappropriate remedy to resolve investors' claims?
	We note that this approach is counter to established law of general property rights. However in these instances we believe it is the right approach to not allow tracing of assets.
36	If you favour keeping tracing as a potential remedy in the case of Ponzi schemes how would you address the issues identified with its application?
	N/A
37	Do you agree that investors should not be able to retain any fictitious profits paid to them?
	No.
38	Do you agree that there should be a limit on the period of a clawback?
	Yes.
39	Do you agree that four years is a reasonable period for a clawback to operate? If not what alternative would you propose?
	No four years is not reasonable. The Clawback period should be 2 years to be aligned with the voidable preference rules under the Companies Act 1993.
40	Do you think that the liquidator of a Ponzi scheme should be able to apply to the courts to extend the period of vulnerability, in respect of specific investors, where it can be shown that the investor received distributions in bad faith?
	Yes.
41	Do you agree that in order to have the benefit of a defence against the clawback powers of the liquidator investors should be required to demonstrate that <i>a reasonable person in their position would not have suspected, and they did not have reasonable grounds for suspecting, that a Ponzi scheme existed?</i> If not, what alternative test would you propose?

	Yes.
42	Do you agree that significant financial hardship is an appropriate criterion for determining whether an investor merits retaining funds received from a Ponzi scheme?
	Yes.
43	Do you consider that alternative criteria should be used for determining whether an investor merits retaining funds received from a Ponzi scheme?
	No.
44	Do you consider that a whistle blower safe harbour should be provided to investors in a Ponzi scheme? If there is to be a safe harbour, do you consider that this should be available to all investors or just the first investor to 'blow the whistle'?
	No. Investors should not be rewarded for blowing the whistle (An early warning might save the whistle blower having a larger loss.)
45	Do you think that a defence should be provided for investors who substantially alter their position in the reasonably held belief that a distribution or withdrawal was valid and would not be set aside?
	Yes.
46	Do you agree that recovery against trade creditors of a Ponzi scheme should continue to be dealt with under the ordinary principles of insolvency law?
	Yes.
47	Do you agree that a proportional distribution of assets is preferable in the case of all Ponzi schemes regardless of the legal structure of the Ponzi scheme?
	Yes.
48	Do you have any information about the cost to find out whether the losses specifically attributable to individual investors are able to be identified?
	Our experience suggests the costs of trying to determine if losses are attributable to individual investors are substantial.
49	Do you agree that investors in a Ponzi scheme should not be entitled to the benefit of any fictitious profits allocated to them when deciding their proportional entitlements to the assets of a Ponzi scheme?
	Yes.
50	What is the most appropriate model for distributing assets?
	No preference as with all models there will be investors that are better off and investors that are worse off. However, we note that the main criteria for any option is to have a clear, consistent and easily understood model which enables everyone to understand their potential liability and

	likely outcome and transparency over process. As stated earlier and below we believe that most appropriate place for the distribution method to be determined is via the Courts.
51	Are there any additional models which we should consider?
	No.
52	Should investors' losses be able to be adjusted to take account of inflation or any other factors?
	No. For simplicity, we believe there should be no inflation adjustment.
53	Are there any additional or alternative criteria which we should use to assess the various models for distributing assets to investors?
	No.

Other comments

As stated earlier we question the need for a specific Ponzi Scheme Regulations. Ponzi scheme are rare in New Zealand and are very fact specific. We believe the current model where a directions are sort from the Court is still the most effective model. This model allows all the stakeholders to have a voice and put their case forward for the distribution model. In our experience, the major cost is not determining the distribution model, but in determining the amounts due to investors and in managing and realising the assets.