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CBL INSURANCE LIMITED (IN LIQUIDATION)

LIQUIDATORS' FIRST REPORT AND NOTICE TO CREDITORS
(PURSUANT TO SECTION 255 AND 245 OF THE COMPANIES ACT 1993)

Company Number: 27532

1. Appointment

Pursuant to an application under Section 246 of the Companies Act 1993 by CBL Insurance Limited's ("CBLI" or "the Company") prudential supervisor, the Reserve Bank of New Zealand ("RBNZ"), the Company was placed into interim liquidation by an Order of the High Court dated 23 February 2018, pending the determination of the RBNZ's liquidation application. Kare Johnstone and Andrew Grenfell were appointed joint and several interim liquidators.

Following a number of adjournments, the RBNZ's application to appoint liquidators to CBLI was heard in the Auckland High Court on 12 November 2018, which resulted in an order by the Court placing the Company into liquidation and the appointment of Kare Johnstone and Andrew Grenfell ("Liquidators") as joint and several liquidators.

A copy of the High Court Order dated 12 November 2018 and the Judgement of Justice Courtney are attached as Appendix 1 to this report.

2. Disclaimer

The purpose of this report is to report to CBLI's creditors and shareholder in accordance with Section 255 of the Companies Act 1993.

This report has been prepared based on the information known to the Liquidators as at the date of this report. We reserve the right (but will be under no obligation) to review this report and if we consider it necessary to revise the report in light of any information existing at the date of this report that becomes known to us after that date. We have not independently verified the accuracy of information provided to us, nor have we conducted an audit in respect of the Company. We express no opinion on the reliability, accuracy, or completeness of information provided to us and upon which we have relied.

The Liquidators do not accept responsibility or liability for any losses occasioned to any party as a result of the circulation, publication, reproduction, or use of this report.

3. Company information

Date of Incorporation:	19 April 1973
Trading address:	Level 8, CBL House, 51 Shortland Street, Auckland
Type of business:	Provision of insurance and reinsurance
Date trading ceased:	23 February 2018

Shareholder:	LBC Holdings New Zealand Limited (In Voluntary Administration)
Ultimate parent:	CBL Corporation Limited (In Voluntary Administration)
Directors at date of liquidation:	Peter Alan HARRIS Alistair Leighton HUTCHISON
Director resignations since the date of interim liquidation:	Anthony Charles Russell HANNON Norman Gerald Paul DONALDSON Sir John WELLS Ian Kelvin MARSH

4. Events leading to appointment of Liquidators

CBLI became a fully licenced insurer in September 2013 and operated under the provisions of the Insurance (Prudential Supervision) Act 2010 ("IPSA") and the prudential oversight of the RBNZ.

In October 2015, CBLI's ultimate parent, CBL Corporation Limited ("CBL Corp"), listed on the New Zealand and Australian stock exchanges.

In mid-2017 the RBNZ identified concerns with the adequacy of CBLI's reserves, in particular in relation to the French builders warranty insurance which the Company reinsured from overseas based ceding insurers Alpha Insurance A/S ("Alpha"), Elite Insurance Limited ("Elite") and CBL Insurance Ireland dac ("CBLIE"), an Irish subsidiary of CBL Corp.

An independent report commissioned in mid-2017 by the Gibraltar Financial Services Commission ("GFSC") into the reserves of CBLI's largest ceding insurer, Elite, concluded that Elite was materially under-reserved in respect of its French construction insurance business reinsured by CBLI. In July 2017 Elite ceased writing business and went into "run-off".

As a result of the issues identified with Elite's French construction insurance business, Alpha's regulator required it to increase its reserves. In addition, the regulator of CBLIE, the Central Bank of Ireland, also raised concerns as to CBLIE's reserves and issued it with a number of directions, including a direction to not make any payments or transfer of assets to any related party of CBLIE, which included payments due to CBLI for reinsurance premiums.

In July 2017 the RBNZ directed CBLI to increase its solvency ratio from 100% to 170% and to not enter into arrangements that provided new or increased levels of financial support to any insurer or reinsurer not owned by CBL Corp.

In August 2017 the RBNZ appointed McGrathNicol to undertake an independent investigation into the financial position of CBLI, including the appropriate level of provisions and reserves for CBLI's French construction business. To assist in assessing the adequacy of CBLI's reserves in relation to the French construction business reinsured by CBLI at 31 December 2017, of which 95% relates to CBLI's three major ceding insurers (Alpha, Elite and CBLIE), independent actuarial experts, Finity Consulting Pty Limited ("Finity") and Milliman France, a global actuarial firm with specific expertise in the French construction market, were engaged.

During September 2017 the Company disclosed that its 30 June 2017 solvency ratio was 132% compared to the 170% required under its licence. In November 2017 the Company, and its Appointed Actuary, PwC, informed the RBNZ that the solvency ratio requirement of 170% was likely to be breached at 31 December 2017. On 21 February 2018 CBLI verbally advised the RBNZ that its solvency ratio had declined from 132% to below 100%. The solvency ratio at 31 December 2017 was 25%.

In November 2017 the directors of CBL Corp advised the RBNZ they were investigating restructuring options. The RBNZ, also in November 2017, issued a direction under IPSA that required CBLI and CBL Corp to consult with it prior to any payment or transfer of assets in excess of $5 million.

CBL Corp issued a market announcement in early February 2018 which stated that CBLI's French business required an increase in reserves of $100 million, of which in excess of $90 million related to years earlier than FY17. The announcement also stated that a $44 million write off of receivables through a related company was required.

On 12 February 2018 the RBNZ issued a direction under IPSA that CBLI was prohibited to make the Company's proposed payment of €25 million to Alpha and also directed that no other payment or transfer of assets of $1 million or more could be made to Alpha, or any other companies within the Alpha Group, without the prior written permission of the RBNZ.

On 16 February 2018, CBLI made a €25 million payment to Alpha in breach of the RBNZ's direction.

The draft independent actuarial valuation undertaken by Finity and Milliman which concluded CBLI had a significant shortfall in its claims reserves, was issued and provided to the Company on 17 February 2018 for its review and comments.

On 21 February 2018 the RBNZ requested information under IPSA in respect of any payment or transfer of assets of $1 million or more made by CBLI, CBL Corp or any of its subsidiaries on or after 1 February 2018.

CBLI disclosed that between 14 and 20 February 2018 it had made total payments of circa $55 million to two specific parties, including the €25 million payment to Alpha on 16 February 2018.

On 23 February 2018 the RBNZ filed a liquidation application with the Auckland High Court requesting the immediate appointment of Interim Liquidators pending the determination of the liquidation application on the grounds that CBLI had breached the 12 February 2018 direction not to make the €25 million payment to Alpha and that the Company was failing to maintain its required solvency margin of 170%.

The Company was placed into interim liquidation on 23 February 2018 with the role of the interim liquidators to preserve the Company's assets until the substantive liquidation application was determined.

Following a number of adjournments, on 12 November 2018 the Auckland High Court ordered the Company be placed into liquidation.

The control and management of the Company remained with the directors and senior management up until the appointment of the interim liquidators as which point control was removed from the directors.

5. Statement of affairs

Management has provided the Liquidators with the unaudited monthly management accounts as at 30 September 2018, being the latest available financial information. An unaudited statement of assets and liabilities as at 30 September 2018 derived from the management accounts, based on the two actuarial assessments (PwC and Finity), is attached as Appendix 2. The Liquidators are not able to express an opinion on the validity of the information provided in the statement of assets and liabilities.

Given the Interim Liquidators were in control of the Company's affairs between 30 September 2018 and the date of liquidation (being 12 November 2018), the position of the Company is unlikely to have materially changed during this period.

6. Analysis of statement of affairs

The Liquidators have made various adjustments to the unaudited statement of assets and liabilities as at 30 September 2018 and these are noted in the unaudited assets and liabilities statement attached as Appendix 2. The Liquidators consider that, regardless of which actuarial valuation is used, the Company was balance sheet insolvent as at 23 February 2018, the date of interim liquidation. The Company may also have been balance sheet insolvent prior to this date. This will be included as part of the Liquidators' investigations into the affairs of the Company prior to liquidation.

7. List of creditors

The High Court order, attached as Appendix 1, granted an exemption to the Liquidators in respect of having to provide a list of creditors with this report, and issuing a copy of this report to all known creditors, due to the large number of creditors.

8. Proposals for conducting the liquidation

The Company is in run-off due to the following primary reasons:

- The Company is balance sheet insolvent;
- The Company is unable to meet the terms of its licence and required solvency margin under IPSA;
- Continuing to write new business would be in breach of the Company's licence, which is a criminal offence;
- The Directors did not get the necessary support from major creditors to restructure and re-capitalise the Company during the eight months preceding the hearing of the RBNZ's liquidation application on 12 November 2018.

The Liquidators will, among other things:

- Control and maintain the value of CBLI's assets;
- Seek to reduce the Company's balance sheet risk, where possible, through appropriate risk transfers, commutations or other mechanisms available to CBLI;
- Collate creditor and policyholder information;
- Continue the ongoing management and processing of claims;
- Understand and clarify the reinsurance position that CBLI has with various insurers internationally;
- Establish the quantum of unsecured creditor claims;
- Realise CBLI's assets and receivables in order to meet unsecured creditor claims;
- Continue to investigate the affairs of the Company and whether or not any claims should be pursued against the directors, officers or others parties, including an investigation into potential insolvent transactions.

At this stage, we intend to carry on with our balance sheet risk reduction strategy throughout the first quarter of 2019. We then anticipate that we should be in a position to write to all creditors and policyholders updating them on the Company's position and potential outcome.

9. Estimated date of completion of liquidation

Given the long tail nature of some of CBLI's insurance policies and the regulatory investigations (Serious Fraud Office, Financial Markets Authority and the RBNZ), that are currently underway, together with the Liquidators' investigations into the affairs of the Company prior to the liquidation, it is not practicable to estimate the date of the completion of the liquidation.

10. Creditors' meeting

A Liquidator may call a meeting of creditors in order to decide whether to appoint a replacement Liquidator.

Having regard to the assets and liabilities of the Company, the likely result of the liquidation and the purpose of the liquidation, the Liquidators consider in accordance with Section 245 of the Companies Act 1993 that no such meeting should be held at this point in time.

A meeting will not be called unless within 10 working days after receiving this notice a creditor gives notice in writing to the Liquidators requiring a meeting to be called.

As noted in paragraph 8 above, the Liquidators are currently conducting a balance sheet liability reduction strategy. Once this risk reduction strategy has been completed, the Liquidators will consider if a Scheme of Arrangement would be in the best interests of all creditors. If the Liquidators decide that is the case, and subject to any Court directions, a meeting of creditors will be convened by the Liquidators to allow the creditors to consider and vote on any proposed Scheme.

11. Liquidation committee

In accordance with Section 314 of the Companies Act 1993 a creditor or shareholder may request the Liquidators call a meeting of creditors or shareholders at any time in the course of the liquidation to vote on a proposal that a Liquidation Committee be appointed to act with the Liquidators. This request must be in writing.

The Liquidators may decline a request by a creditor or a shareholder to call a meeting on the ground that the:

a) request is frivolous or vexatious; or

b) request was not made in good faith; or

c) costs of calling the meeting would be out of proportion to the value of the Company's assets.

The decision to decline a request may be reviewed by the Court on the application of any creditor or shareholder.

12. Liquidators' remuneration

The Court order included approval from the High Court of the Liquidators' fee rates applicable to the liquidation. Under Section 284(1)(e) of the Companies Act 1993 creditors or shareholders are entitled to have the Liquidators' remuneration reviewed by the Court.

13. Creditors' claims

Personal Property Securities Act / Reservation of Title

Should any creditor believe that they have registered a Purchase Money Security Interest on the Personal Property Securities Register over any goods, or proceeds from realisation for goods, they should contact this office immediately.

If any creditor believes that they have a Retention of Title over goods and they have not registered their interest on the Personal Property Securities Register, they should also contact this office immediately. Suppliers of consignment or sale or return stock should also contact this office immediately.

Creditors' claim forms

We are not calling for claims at this point in time. However, a call for claims will be made prior to the creditors' meeting referred to in paragraph 10 of this report.

Should you consider you are a secured creditor of the Company would you please contact the Liquidators and they will supply to you a secured creditor's valuation and claim form.

14. Further information

Should you have any information that you believe would lead to realisations for the benefit of creditors, please set it out in writing, attaching copies of all documentary evidence, and send it to the Liquidators. Please note that the Liquidators can only act on written information as telephone, or other conversations will be regarded as hearsay by the Court.

15. Prospect of dividend

It is too early in the liquidation to estimate the dividend that could be paid to unsecured creditors. The Liquidators expect to be in a position to provide an update to creditors in this regard in their next statutory report.

16. Contact details

The Liquidators can be contacted at McGrathNicol, Level 17, 34 Shortland Street, Auckland, (PO Box 106-733, Auckland 1143). Telephone enquiries should be directed to Helen Gair, direct dial (09) 926 5111.

Dated: 17 December 2018

Kare Johnstone
Liquidator

Andrew Grenfell
Liquidator

Appendix 1

i) High Court Order

DUPLICATE

IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

I TE KŌTI MATUA O AOTEAROA
TĀMAKI MAKAURAU ROHE

CIV 2018-404-306

Under	Part 4 of the Insurance (Prudential Supervision) Act 2010 and Part 16 of the Companies Act 1993
In the matter of	an application to appoint liquidators to the defendant company
Between	**RESERVE BANK OF NEW ZEALAND**, a bank constituted pursuant to the Reserve Bank Act 1989, acting as prudential supervisor of insurance business in New Zealand
	Plaintiff
And	**CBL INSURANCE LIMITED** a company having its registered office at Level 8, 51 Shortland Street, Auckland, New Zealand and carrying on business there and elsewhere as an insurer and reinsurer
	Defendant

ORDERS OF JUSTICE COURTNEY
(A) APPOINTING LIQUIDATORS TO THE DEFENDANT COMPANY;
(B) FIXING RATES OF REMUNERATION OF LIQUIDATORS;
(C) UNDER SECTIONS 255 AND 257 COMPANIES ACT 1993.
Dated: ~~15~~ 16th November 2018

REGISTRAR OF HIGH COURT AUCKLAND N.Z.

THE SEAL OF THE HIGH COURT NEW ZEALAND

BUDDLEFINDLAY
NEW ZEALAND LAWYERS
Barristers and Solicitors
Wellington

Solicitor Acting: **Scott Barker/Bridie McKinnon**
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ORDERS OF JUSTICE COURTNEY
(A) APPOINTING LIQUIDATORS TO THE DEFENDANT COMPANY;
(B) FIXING RATES OF REMUNERATION OF LIQUIDATORS;
(C) UNDER SECTIONS 255 AND 257 COMPANIES ACT 1993.

1. The application made by the plaintiff, the Reserve Bank of New Zealand, was determined by Her Honour Justice Courtney on Monday, 12 November 2018 at 3pm.

2. This Court orders that:

   (a) The defendant company be put into liquidation by the Court under the Companies Act 1993, and appoints Kare Johnstone and Andrew John Grenfell as liquidators.

   (b) The requirements under ss 255(2)(c)(ii) and (d) and 257(1) of the Companies Act 1993 ("Act") relating to the sending of the liquidators' reports and all other documents required to be sent under those sections (together, the "Liquidators' Reports"), be modified such that:

      (i) the Liquidators' Reports be uploaded to the website of McGrathNicol at https://www.mcgrathnicol.com as soon as practicable after they have been prepared.

      (ii) the sealed orders in this proceeding be sent to every known creditor and shareholder of the entities that are the subject of this application at the same time and in the same manner (as modified by 2(b) above) as the documents listed in s 255(2)(c)(ii) of the Act.

   (c) The Court approve the hourly rates of the applicants as liquidators of the entities that are the subject of this application as follows (exclusive of GST and expenses):

Position	**Rate**
Partner	$640 per hour
Director	$545 per hour
Senior Manager	$475 per hour
Manager	$415 per hour
Assistant Manager	$365 per hour
Senior Analyst	$295 per hour
Analyst	$280 per hour
Administrator	$275 per hour
Secretary	$170 per hour

THE SEAL OF THE HIGH COURT NEW ZEALAND

(d) Leave be reserved to the applicants to apply from time to time, but not more frequently than 6-monthly, for approval of other rates, any such application being supported by affidavit evidence of the applicants deposing to the rates.

(e) The orders be made subject to the power of the Court to review the overall remuneration of the applicants as liquidators of the Company under section 284(1)(e) of the Companies Act 1993 and to order a refund of the remuneration under section 284(1)(f) of that Act.

(f) The liquidators notify every known creditor and shareholder of the entities that are the subject of this application of the liquidators' rates of remuneration approved by the Court in the liquidators' next reports under s 255(2) of the Companies Act 1993, subject to the modifications set out above at 2(b).

(g) Leave is reserved for the applicants to apply further in respect of any ancillary orders.

3. Before making these orders, the Court—

(a) heard N Gedye QC and S Barker for the plaintiff, D Salmon for the defendant company, M Kersey for LBC Holdings New Zealand Limited, A Ross QC and J Lethbridge for Elite Insurance Company Ltd, J Anderson QC and J McGillivray for Alpha Insurance A/S, J Cooper QC and A Murray for the interim liquidators and H Quinlan for Curmi and Partners Ltd.

(b) read the statement of claim and the affidavit Toby Jonathan Twisleton-Wykeham Fiennes verifying the allegations in the statement of claim; and

(c) sighted the advertisements for the statement of claim published in *The New Zealand Gazette* on Wednesday, 4 April 2018 and in *The New Zealand Herald* on Wednesday, 4 April 2018.

REGISTRAR OF HIGH COURT AUCKLAND N.Z.

Date: 16th November 2018

S Tuiaana'e

(Deputy) Registrar

THE SEAL OF THE HIGH COURT NEW ZEALAND

ii) **Amended Judgment of Justice Courtney dated 12 November 2018**

IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

I TE KŌTI MATUA O AOTEAROA
TĀMAKI MAKAURAU ROHE

CIV-2018-404-000306
[2018] NZHC 2969

UNDER	Part 4 of the Insurance (Prudential Supervision) Act 2010 and Part 16 of the Companies Act 1993
IN THE MATTER OF	an application to appoint liquidators to the defendant company
BETWEEN	RESERVE BANK OF NEW ZEALAND Plaintiff
AND	CBL INSURANCE LIMITED Defendant

Hearing: 12 November 2018

Appearances: N S G Gedye QC and S A Barker for Reserve Bank
J S Cooper QC and A E Murray for Interim Liquidators
A S R Ross QC and J E M Lethbridge for Elite Insurance
M Kersey for LBC Holdings
J A MacGillivray for Alpha
D A Salmon and J P Cundy for CBLI
H L Quinlan for Supporting Creditor

Judgment: 16 November 2018

JUDGMENT OF COURTNEY J

This judgment was delivered by Justice Courtney
on 16 November 2018 at 2.30 pm
pursuant to R 11.5 of the High Court Rules

Registrar / Deputy Registrar

Date.....

Introduction

[1] On 12 November 2018, I made an order placing CBL Insurance Ltd (in interim liquidation) (CBLI) in liquidation. The liquidation application had been made by the Reserve Bank of New Zealand (the Bank) in its capacity as regulator under s 151(2) of the Insurance (Prudential Supervision) Act 2010 (IPSA). This was the first such application decided under s 151(2). For that reason, and because of the high level of public interest in the demise of CBLI, it is appropriate to give reasons for my decision.

[2] The liquidation application proceeded unopposed and with the active support of CBLI's largest creditor, Elite Insurance Company Ltd (Elite). However, that state of affairs only came about on the morning of the hearing. Since the appointment of Interim Liquidators, in February 2018 there had been strenuous efforts to oppose liquidation. The company (represented by two of its directors, Peter Harris and Alistair Hutchison) and its shareholder, LBC Holdings Ltd (administrators appointed) (LBC), had maintained that voluntary administration pursuant to a Deed of Company Arrangement (DoCA) would be preferable to liquidation. LBC withdrew its opposition two days before the hearing and CBLI and the directors only withdrew their opposition on the morning of the hearing.

[3] Two other creditors appeared. Alpha Insurance A/S (in bankruptcy), CBLI's second largest creditor appeared and abided the Court's decision. Curmi and Partners Ltd appeared and abided the decision of the Court.

[4] The Interim Liquidators also appeared, to assist the Court. They abided the decision.

The statutory context: the Insurance (Prudential Supervision) Act 2010

[5] The IPSA came into force in 2010. Its purposes are to promote the maintenance of a sound and efficient insurance sector and to promote public confidence in the insurance sector.[1] To those ends, the IPSA establishes a licencing system for insurers and imposes prudential requirements. The Bank is responsible for compliance with

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[1] Insurance (Prudential Supervision) Act 2010, s 3(2).

those requirements and has certain powers in respect of insurers that are in financial distress or which have breached their prudential requirements.[2]

[6] Section 4 of the IPSA identifies a number of principles that the Bank must take into account in carrying out its statutory functions and exercising the powers conferred on it by the IPSA. Relevantly, they include:

> …
>
> (b) The importance of maintaining the sustainability of the New Zealand insurance market.
>
> (c) The importance of dealing with an insurer in financial distress or other difficulties in a manner that aims to –
>
> (i) adequately protect the interests of its policy holders and the public interest; and
>
> …
>
> (i) Desirability of sound governance of insurers.

[7] Section 151 of the IPSA permits the Bank to apply for an order that a licensed insurer be placed in liquidation. That section provides:

> (1) The Bank may, in the case of a licensed insurer that may be put into liquidation under or in accordance with the Companies Act 1993, apply to the High Court to appoint a liquidator for the insurer.
>
> (2) The High Court may, on an application under subsection (1), appoint a liquidator for the licensed insurer if it is satisfied that –
>
> (a) the insurer is unable to pay its debts (and, for that purpose, section 287 of the Companies Act 1993 applies with all necessary modifications whether or not the insurer is a company); or
>
> (b) the insurer is failing to maintain a solvency margin; or
>
> (c) the insurer has persistently or seriously failed to comply with any direction, condition, or other requirement imposed by or under this Act or the regulations; or
>
> (d) it is just and equitable that the insurer be put into liquidation.

[8] The Bank does not assert that CBLI is unable to pay its debts as they fall due. Its application was brought under s 151(2)(b), (c) and (d), asserting that:

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[2] Insurance (Prudential Supervision) Act 2010, s 3(2).

(a) CBLI was in breach of its required solvency margin;

(b) CBLI had seriously failed to comply with directions given by the Bank in 2017 and early 2108;

(c) it was just and equitable to wind CBLI up because it was balance sheet insolvent and because of impropriety by the directors.

Background

[9] CBLI is part of the wider CBL group. It is a subsidiary of LBC, which is, in turn, owned by CBL Corporation Ltd (New Zealand) (CBL Corp). CBL Corp is listed on the NZX and ASX. CBLI is the group's largest operating entity. It is a licensed insurer in New Zealand, though almost all its business is written overseas; only approximately one per cent of its business (by premium) relates to New Zealand risks.

[10] CBLI was heavily exposed as a reinsurer to builders' warranty insurance written in France. Such insurance, which is compulsory, protects both builders and home owners in respect of construction defects. It is regarded as long-tail because the statutory claims notification period extends for 10 years. Elite, an insurer based in Gibraltar, ceded some 80 per cent of the French construction policies it wrote to CBLI under a quota share arrangement. Alpha also underwrote these risks and ceded approximately 90 per cent of them to CBLI. Elite and Alpha between them represent some 80 per cent of the CBLI's outstanding claims liability. CBLI also accepted cessions of these risks from CBLI Europe Ltd (CBLIE), another company in the CBL group. The French business had grown significantly since 2006. Gross written premia for these products increased from $1 million in 2006 to $38 million in 2011 to $130 million in 2016.

[11] During 2016 there was ongoing engagement between the Bank, CBLI and the company's appointed actuary, PwC NZ. The Bank had concerns about CBLI's rapid business expansion, reserving strategy and adequacy of reserves. These concerns intensified with events affecting the ceding insurers. By early 2017, Elite's regulator, the Financial Services Commission of Gibraltar (FSCG) was concerned about aspects of Elite's business, including the adequacy of reserving for the French insurance business and its exposure to CBLI. It required Elite to cease issuing and renewing

policies. In July 2017, Alpha's regulator, the Danish Financial Supervisory Authority, required Alpha to substantially increase its claims provision as a result of concerns about the company's exposure to the French construction business reinsured by CBLI. Further, CBLI's sister company, CBLI Europe Ltd (CBLIE) was required by its regulator, the Central Bank of Ireland, to strengthen its balance sheet, which led to CBLIE withholding reinsurance premia from CBLI.

[12] The Bank was sufficiently concerned to write to CBLI on 25 July 2017 recording its belief that it had reasonable grounds to conclude that CBLI may not be carrying on its business in a prudent manner and invoking its power under s 130 of the IPSA to initiate an investigation. It gave directions requiring CBLI not to enter into any transaction or transactions that would have the effect of increasing its exposure to Elite and required it to maintain a solvency ratio of 170 per cent.

[13] The liquidation application arose from the events that followed.

The liquidation application

Solvency margin

[14] Under s 55 of the IPSA, the Bank may issue solvency standards. Such standards may be general or specific[3] and may prescribe the minimum amount of capital that an insurer must hold and maintain and the methods for calculating that amount of capital.[4] A licensed insurer may also be required to maintain a minimum solvency margin (a prescribed dollar amount) or a minimum solvency ratio (a percentage buffer) in accordance with the applicable solvency standard.[5]

[15] A licensed non-life insurer, which CBLI was, is also required to submit solvency returns to the Bank on a half-yearly basis.[6] If a licensed insurer has reasonable grounds to believe that a failure to maintain the solvency ratio is likely to occur at any time within the following three years, it must report that likely failure to

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3 Section 55(3).
4 Section 56.
5 Insurance (Prudential Supervision) Act 2010, s 21(b).
6 Solvency Standard for Non-Life Business 2014, s 4.2 and Insurance (Prudential Supervision) Act 2010, s 81(1) and (2).

the Bank as soon as reasonably practicable.[7] A licensed insurer must also have an actuary appointed by the insurer.[8]

[16] In November 2017, CBLI and its appointed actuary advised the Bank that the company was likely to breach its solvency ratio at 31 December 2017. Given that development and in light of breaches of directions given by the Bank (to which I come shortly) the Bank applied in February 2018 to have interim liquidators appointed. The Insurer Solvency Return filed in March 2018 showed the solvency ratio as at December 2017, at 25 per cent.

[17] The seriousness of the breach and the circumstances in which it arose were acknowledged by CBLI and were such that it would, in itself, have justified winding up. However, I also considered the other grounds on which the Bank relied and go on to consider them as well.

Serious breach of Bank's directions

[18] On 22 November 2017, the Bank issued a modified direction requiring CBLI to consult with the Bank before entering any transaction or series of related transactions that involved the payment or transfer of assets of $5 million or greater. That direction was further modified in late January 2018 to clarify the consultation requirement so that the direction required that:

> CBL Insurance Ltd must prior to entering any transaction or series of related transactions involving payment or transfer of assets of NZ$5 million or greater consult with the Reserve Bank about its circumstances and about the transaction or any other actions or proposed actions it intends to take in resolving its difficulties. Consult means – providing the Reserve Bank with sufficient information for the Reserve Bank to form an informed view on the proposed transaction, receiving feedback from the Reserve Bank, and having regard to that feedback before entering a transaction.

[19] In early February 2018, a trading halt was ordered on CBL Corp's shares pending an announcement on its financial result for the 2017 year which included a forecast loss of NZ$75 – 85 million after tax. This situation was attributed largely to the need to increase its reserve for the French construction business by approximately

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7 Insurance (Prudential Supervision) Act 2010, s 24.
8 Insurance (Prudential Supervision) Act 2010, s 76.

$100 million. However, just over a week later, CBL Corp announced its withdrawal from the French construction business.

[20] At the same time, the Bank became aware of CBLI's intention to make a payment of €25 million to Alpha in relation to reinsurance claims. The Bank instructed CBLI verbally, on 11 February 2018, not to make the payment. The verbal instruction was followed by written directions on 12 February 2018 that:

> CBL Insurance Ltd must not without the prior written permission of the Reserve Bank enter into any other transaction or series of related transactions involving payment or transfer of assets of NZ$1 million or greater to Alpha Insurance A/S or any other companies in the Alpha Insurance group. For the avoidance of doubt this includes any backdated transaction.

[21] CBLI wrote to the Bank on 15 February 2018 expressing its very serious concerns about the consequences of not making the €25 million payment to Alpha and asking the Bank to reconsider its decision. The Bank responded the following day, refusing to agree to the payments being made. Nevertheless, between 8 and 20 February 2018, CBLI made six payments that totalled approximately NZ$55 million. These included a payment of €25 million to Alpha.

[22] In his affidavit sworn on 23 May 2018, Mr Harris acknowledged that CBLI had made the payments. His explanation for doing so was simply that "there were important commercial reasons for the payments and I consider it was in the interests of CBLI to make them".

[23] Given the clarity of the Bank's directions regarding such payments and the circumstances in which they were made, there can be no doubt that there was a serious failure to comply with the directions.

The just and equitable ground

[24] The just and equitable ground, although typically relied on in the context of winding up under the Companies Act 1993 in cases involving disputes between shareholders, is not limited to such cases. In *Baird v Lees*, Lord President Clyde declined to attempt a definition of the circumstances that might amount to a just and equitable cause but said:[9]

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[9] *Baird v Lees* 1924 SC 83 at 90.

> A shareholder puts his money into a company on certain condition. The first of them is that the business in which he invests shall be limited to certain definite object. The second is that it shall be carried on by certain persons elected in a specified way. *And the third is that the business shall be conducted in accordance with certain principles of commercial administration defined in [the relevant statute] which provide some guarantee of commercial probity and efficiency*.
>
> (emphasis added)

[25] The Privy Council adopted those observations in *Loch v John Blackwood Ltd*:[10]

> Such a consideration, in their Lordships' view, ought to proceed upon a sound induction of all the facts of the case, and should not exclude, but should include circumstances which bear upon the problem of continuing or stopping courses of conduct which substantially impair those rights and protections to which shareholders, both under statute and contract, are entitled. *It is undoubtedly true that at the foundation of applications for winding up on the "just and equitable" rule there must lie a justifiable lack of confidence in the conduct and management of the company's affairs*. But this lack of confidence must be grounded on conduct of the directors, not in regard to their private life or affairs, but in regard to the company's business. Furthermore, the lack of confidence must spring not from dissatisfaction at being out-voted on the business affairs or on what is called the domestic policy of the company. *On the other hand, wherever the lack of confidence is rested on a lack of probity in the conduct of the company's affairs, then the former is justified by the latter, and it is under the statute just and equitable that the company be wound up*.
>
> (emphasis added)

[26] It is evident from these cases that conduct amounting to a lack of probity such as to warrant winding up on the just and equitable ground need not involve illegality. The question for the Court is whether the justice and the equity of the case requires that outcome.[11] Matters of illegality are, self-evidently, for another forum.

[27] Where a liquidation application is brought by the Bank as regulator under the IPSA, the considerations just described must be viewed with the purposes and principles of the IPSA in mind. The Bank's concern is not limited to the interests of policy holders but takes in the broader objective of maintaining a sound and efficient insurance sector and promoting public confidence in the insurance sector. An important aspect of that, which it is required specifically to take into account, is the sound governance of insurers.

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[10] *Loch v John Blackwood Ltd* [1924] AC 783 at 788, cited in *Re Livestock Investments Ltd* Supreme Court Auckland M525/77, 18 December 1978 in relation to an application by the Registrar of Companies under s 219 of the Companies Act 1955.

[11] *Secretary of State for Business Innovation and Skills v PAG Management Services Ltd* [2015] EWHC 2402 (Ch).

[28] Importantly, these considerations apply even in relation to insurers that seek to be licenced in New Zealand while writing most or even all of their business overseas. In its report to the Finance and Expenditure Committee on the Insurance (Prudential Supervision) Bill dated 22 February 2010, the Bank noted the importance of its commitment to international co-operation in relation to the regulation of multi-national corporations and the need to not undermine that position. That means ensuring that off-shore regulators are not undermined and New Zealand does not become a haven for offshore insurers by being perceived as a "softer" regulatory jurisdiction.

[29] The two aspects relied on by the Bank in asserting that it was just and equitable to wind CBLI up were first, that CBLI was "balance sheet insolvent" and, secondly, misconduct in the management of the company.

[30] The company's financial position would not have brought the case within s 151(2)(a), which requires the company not to be able to pay its debts (cashflow insolvency). But the Bank submitted that, in the context of an insurance company the test of cashflow insolvency is of limited use; an immediate cashflow shortage is rarely the reason for an insurer's insolvency and an insurer that is able to meet its day-to-day debts immediately may nevertheless be insolvent. The Bank asserted, however, that CBLI's liabilities substantially exceeded its assets, so that it was balance sheet insolvent, which was significant given that its largest exposure lies in future long-tail claims.

[31] Mr Gedye submitted that the importance of balance sheet insolvency risked those whose claims arose in the near future being paid in full at the expense of those whose claims arose in the more distant future, a point also made in *Insurance Commissioner v Associated Dominions Assurance Society Pty Ltd.*[12] In *ASIC v Bilkurra Investments Pty Ltd*, Beach J accepted that balance insolvency could be taken into account in considering the just and equitable ground.[13]

[32] I accepted that the balance sheet position was a matter that could be taken into account in considering this aspect of the Bank's application. The state of CBLI's

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12 *Insurance Commissioner v Associated Dominions Assurance Society Pty Ltd* (1953) 89 CLR 89. See also *New Cap Reinsurance Corporation v A E Grant* [2008 NSWSC 1015 at [74].

13 *ASIC v Bilkurra Inveatments Pty Ltd* [2016] FCA 371.

balance sheet was the subject of considerable debate over the last several months. Finity, the actuary engaged by the Interim Liquidators, considered that CBLI's liabilities exceeded its assets by NZ$98.4 million as at 31 December 2017. In an affidavit sworn by one of the Interim Liquidators, Ms Johnstone, on 9 November 2018, an updated balance sheet based on Finity's figures showed that, as at 30 June 2018, CBLI's liabilities exceeded its assets by between $122,813,064 and $274,815,430. It is notable that, although Finity's figures have always been rejected by CBLI in favour of the lower PwC figures, the appointed actuary has never provided evidence to support that assertion.

[33] I proceeded on the basis that there is a significant deficit in CBLI's asset position. For an insurer facing substantial long-tail exposure this is a matter of serious concern. The evidence suggested a state of affairs in which the company would be unable to meet its medium to long-term obligations. Those obligations were very significant and would require immediate and competent management. The position was so serious that I would have considered this ground made out without going further. But the allegations of misconduct by the directors, on which the Bank also relied, put the matter beyond doubt.

[34] The Bank filed extensive evidence on this aspect, which I had considered prior to the hearing. In oral submissions, Mr Gedye focused on five transactions which the Bank said showed a level of serious misconduct and impropriety that justified winding up on the just and equitable ground. For present purposes, I think it necessary to refer to only three of these.

[35] The first relates to €12.5 million (approximately NZ$20 million) shown in CBLI records, including its insolvency returns to the Bank, as being a deposit with the National Bank of Samoa (NBS). When the Interim Liquidators requested repayment of the deposit they were advised that the funds were deposited as part of a lending transaction and had been applied to the credit of NBS' customer by way of set-off following the Interim Liquidators' appointment. Enquiries showed that the deposit was part of a series of transactions by which approximately NZ$30 million in reinsurance security reserves held by Alpha were released to CBLI in return for CBLI facilitating a loan of €12.5 million to Alpha. The funds were lent by NBS to Federal Pacific Group (Singapore) Pte Ltd (FedPac), a company associated with

Mr Hutchison, and on-lent by FedPac to Alpha. CBLI issued a surety bond to NBS for the NBS/Fedpac loan and the deposit was held by NBS as cash collateral to support that bond.

[36] The focus for the Bank was a letter held by CBLI from the Chief Executive of NBS, dated 23 March 2015, recording the fact that the CBLI deposit was neither secured nor encumbered and could be returned to CBLI at any time. The Interim Liquidators' investigations indicated that the letter had been requested by CBLI's auditors but was drafted by Mr Harris with involvement from Mr Hutchison and then provided to NBS to sign and return, which NBS did, with one minor amendment. But the letter did not accurately reflect the arrangement between the parties as described. The letter was relied on by the auditors in preparing CBLI's financial statement and by CBLI in relation to its solvency margin discussions with the Bank and the Financial Markets Authority.

[37] The true status of the deposit had significant adverse effects on CBLI's solvency margin. The recalculation of the solvency returns for 31 December 2014 and 30 June 2015 put the true solvency ratio below 100 per cent. This put CBLI in breach of its licence terms on both dates. Notably, CBL Corp was the subject of an Initial Public Offering in October 2015, at which time both Mr Harris and Mr Hutchison sold significant parcels of shares.

[38] The second ground of alleged misconduct and impropriety related to an investment in a goldmine in Peru known as El Toro. On the basis of email communications between Mr Harris and other parties to that investment, the Bank asserts that a parcel of shares in the goldmine were beneficially owned by CBLI but that US$600,000 in dividends paid in respect of the shares had not been received by CBLI. There are other aspects of the El Toro goldmine referred to in the evidence which, the Bank says, raises questions as to whether the goldmine was part of a money-laundering operation and, if so, whether the directors of CBLI appreciated that. It is unnecessary for me to consider those aspects of the evidence. In his oral submissions, Mr Gedye emphasised the recovery aspect of the dividends and value of the shares.

[39] The third area of alleged serious misconduct and impropriety was the proposed sale of CBLI receivables to Castlerock. This related to a managing general agent, SFS,

which was part of the CBL group. CBLI wrote business in the French construction market through SFS and, by late 2017, had $44 million in overdue receivables from that business. Including Elite's share of the receivables and SFS fees, the figure was €88 million. Sometime in September 2017, the CBL group proposed that the receivables be sold for approximately €42.3 million to Castlerock Receivables Management Ltd. The terms of the proposed agreement were recorded in a Term Sheet signed 10 October 2017.

[40] The transaction was entered into at a time when CBLI was already under investigation for conducting its business other than in a prudent manner, but was back-dated to 31 July 2017. In addition, the transaction indicated that CBLI had substantial receivables dating back as far as 2010. Moreover, during the negotiation period of the transaction, CBLI gave notification of its probable breach of the solvency ratio and, when the transaction was cancelled in February 2018, it wrote off the entire amount from its balance sheet. The Bank asserted that the whole transaction was contrived to manipulate the solvency standard rather than substantively improving CBLI's financial position.

[41] For the purposes of the liquidation application, I was satisfied that there had been aspects of CBLI's management that indicated a lack of commercial probity. The transactions described above suggested a preparedness to manipulate records on which third parties, including the regulator, relied. They suggested a lack of candour in dealing with the company's auditors and the regulator. The Bank asserted that, in these circumstances, it was justified in expressing a lack of confidence in the conduct and management of the company's affairs and I agree. I was satisfied that it was just and equitable that CBLI be wound up.

P Courtney J

Appendix 2

CBL Insurance Limited (In Liquidation)			
Statement of unaudited assets and liabilities as at 30 September 2018			**NZ'$000**
	Management accounts (Note 1) (Based on PwC valuation)	**Management accounts (Note 2) (Based on Finity assessment)**	
		Low	**High**
ASSETS			
Cash and cash equivalents	192,668	192,668	192,668
National Bank of Samoa deposit recovery	21,858	21,858	21,858
Reinsurance collateral and claim funds	204,036	204,036	204,036
Insurance receivables	142,134	142,134	142,134
Intercompany receivables	14,594	14,594	14,594
Other receivables	1,224	1,224	1,224
Current tax asset	14,461	14,461	14,461
Loan - CBL Corporation Ltd	4,138	4,138	4,138
Recoveries on outstanding claims	202,834	276,628	319,701
Deferred reinsurance expense and acquisition costs	17,226	17,226	17,226
Deferred tax asset	35,170	35,170	35,170
Fixed assets	1,563	1,563	1,563
Intangible assets	1,983	1,983	1,983
Total Assets	853,889	927,683	970,756
LIABILITIES			
Creditors	40,706	40,706	40,706
Unearned premium liability	56,441	56,441	56,441
Outstanding claims liability	704,160	940,767	1,139,807
Total liabilities	801,307	1,037,914	1,236,954
NET ASSETS / (LIABILITIES) BEFORE LIQUIDATORS' ADJUSTMENTS	52,582	(110,231)	(266,198)
LIQUIDATORS' ADJUSTMENTS (Note 3)	(77,743)	(77,743)	(77,743)
ADJUSTED NET ASSETS / (LIABILITIES) AS AT 30 SEPTEMBER 2018	**(25,161)**	**(187,974)**	**(343,941)**

Source: Management draft unaudited 30 September 2018 financial report and Finity assessment at 30 September 2018

Important Note and Disclaimer:

The above summary has been prepared from information provided by the Company. This information has not been verified. Furthermore, the Liquidators have not carried out an audit of the information supplied and do not accept any responsibility for the accuracy or completeness of the information. The Liquidators do not accept any responsibility on any ground whatsoever, including liability in negligence, to any person.

Notes

1. The outstanding claims liability and recoveries on outstanding claims are based on PWC's valuation as at 31 December 2017 and Management's insurance model reflecting movements to 30 September 2018.
2. The outstanding claims liability and recoveries on outstanding claims are based on Finity's valuation as at 31 December 2017 and movements to 30 September 2018.
3. The Liquidators' adjustments reflect a prudent assessment in respect of the recoveries that relate to National Bank of Samoa, intercompany balances, deferred tax and intangibles. It does not include any adjustments to reflect uncertainty in respect of the collectability of reinsurance receivables, and other assets, at this point in time.