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email lawlex helpdesk.asiapac@saiglobal.com

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Editor: Professor Ian Ramsay, Director, Centre for Corporate Law and Securities Regulation

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1. Recent Corporate Law and Corporate Governance Developments

Next Section

1.1 Government introduces Bill to facilitate administrative winding up of abandoned companies

On 15 February 2012, the Government introduced into Parliament the Corporations Amendment (Phoenixing and Other Measures) Bill 2012 ('the Bill'), to amend the Corporations Act 2001.

The Bill contains two key sets of measures:

(i) Administrative winding up of abandoned companies

The proposed legislation will strengthen the powers of the Australian Securities and Investments Commission (ASIC) to place companies into liquidation when they have been abandoned by their directors.

If a failed company has been abandoned but has not yet been deregistered, employees (or ASIC on their behalf) currently have to apply to the courts and incur legal costs in order to place the abandoned company into liquidation before they can access the Government's employee assistance scheme, the General Employee Entitlements and Redundancy Scheme ('GEERS').

The GEERS aims to protect workers' entitlements in these situations, so that employees of failed companies can recoup many of their unpaid entitlements as quickly as possible.

In addition, where the abandoned company has been deregistered by ASIC or by its members, ASIC or the company's employees have to apply to the courts to reinstate the company and, only once the company is reinstated so that it can be placed into liquidation, could any potential employee eligibility for GEERS be triggered.

To address this impediment, the proposed legislation will provide ASIC with the following discretionary powers:

the power to place a company into liquidation in circumstances where ASIC currently has a power to deregister the company;

the power to reinstate any deregistered company and immediately place it into liquidation; and

the power to place a company into liquidation where ASIC has reason to believe that the company is no longer carrying on business; where ASIC gives notice to the company and its directors of its intention to place the company into liquidation; and where neither the company nor its directors oppose the placement of the company into liquidation.

(ii) Publication of corporate insolvency notices

The Bill will amend the Corporations Act to remove the requirement for public notices in corporate external administrations to be published in newspapers or the ASIC Gazette. Instead, the Bill requires these notices to be published in a "prescribed manner" and provides a power for regulations to be made that will prescribe that manner. These amendments will facilitate the future provision of corporate external administration notices via a single website.

Currently, there are significant costs to external administrations in complying with public disclosure obligations. These costs are ultimately borne by creditors through reduced returns. There are also costs to creditors in monitoring numerous newspapers for relevant notifications - particularly as there is no set newspaper or day of the week on which notices must be published.

As part of the reform package to modernise and harmonise Australia's insolvency industry, the Government in December 2011 announced that ASIC would establish a corporate external administration notices website by 1 July 2012. Online publication of notices will replace approximately 53,000 newspaper advertisements over the next four years, saving external administrations around $15 million over that same period.

The reforms will apply to both advertisement requirements and gazettal requirements.

The Bill is available on the Comlaw website.

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1.2 Government proposes limited recourse borrowings by superannuation funds

On 13 February 2012, the Government announced its proposal to amend the Corporations Regulations 2001 to provide that certain borrowing arrangements by superannuation fund trustees permitted by the Superannuation Industry (Supervision) Act 1993 ('the SIS Act') are financial products under the Corporations Act 2001 ('the Corporations Act').

Generally, superannuation funds are not permitted to borrow funds except in limited circumstances. Superannuation funds are regulated under the SIS Act. Limited recourse borrowing arrangements, such as instalment warrants, are one of the exceptions permitted under the SIS Act, under subsections 67A and 67B.

A previous draft of these Regulations was released for public consultation in June 2010. They have been substantially revised in the light of submissions and other developments. The revised draft regulations are available for public comment for a four week period.

The proposed Corporations Amendment Regulations 2012 ('proposed Regulations') would make limited recourse borrowing arrangements financial products under the Corporations Act when entered into by regulated superannuation funds.

The proposed Regulations amend the Corporations Regulations 2001 to provide that:

limited recourse borrowing arrangements are financial products under the Corporations Act when acquired by superannuation funds;

limited recourse borrowing arrangements are not a credit facility under the Corporations Act when acquired by superannuation funds; and

an Australian Financial Services Licence covering securities or derivatives is taken to also cover limited recourse borrowing arrangements.

The full text of the proposed Regulations is available on the Treasury website.

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1.3 Study of shareholder voting on remuneration reports and 'no vacancy' resolutions

On 10 February 2012, governance advisors Ownership Matters released research showing that fewer S&P/ASX 300 company remuneration reports were defeated during the 2011 AGM season than during any season since 2006, even as almost 12 percent of the first batch of Top 300 reports received a first strike.

The focus on companies receiving a strike under the changes to the Corporations Act 2001 - a vote against the remuneration report of 25 percent or more - obscured the fact just two remuneration report resolutions were defeated in 2011 down from nine in 2010. At least three have been defeated every AGM season since 2006.

The two companies to suffer defeats in 2011 were Crown and Pacific Brands; another 23 S&P/ASX 300 Australian entities experienced 'against' votes of more than 25 percent on publicly available data. The latter included Emeco Holdings, which subsequently disclosed that following a vote audit the number of against votes put it below the 25 percent threshold, and Dexus Property Group, which is not subject to the two strikes legislation but voluntarily submits a remuneration report to investors.

The average vote against a remuneration report of an S&P/ASX 300 company in the six months to 31 December 2011 was 10.4 percent. This average 'against' vote was relatively constant across the 300: from 9.5 percent for S&P/ASX 100 companies to 11.8 percent for those ranked 101 to 200 and 10 percent for the cohort ranked 201 to 300.

Focus on remuneration report votes also obscured the strong investor opposition to attempts by company boards to amend their constitutions to frustrate a less prominent change to the Corporations Act that also came into force on 1 July 2011. These changes ended the ability of a board to unilaterally declare 'no vacancy' on the board in the face of a dissident nominee seeking election regardless of the maximum number of directors permitted under the constitution approved by shareholders.

A 'no vacancy' declaration means a dissident candidate must receive not only a majority of votes cast to be elected but more votes than one of the incumbent directors. A total of seven S&P/ASX 300 companies had attempts to amend their constitutions rejected by shareholders after they attempted to either reduce the number of directors on the board to the number presently in office (or just above the number presently in office) or impose additional requirements on candidates seeking election to the board.

Of the 54 resolutions put by S&P/ASX 300 companies seeking constitutional changes in the last six months of 2011, nine were defeated.

The average vote in favour of an S&P/ASX 300 director was 95.7 percent and just two directors were voted from office during the period - both apparently after disputes with major shareholders.

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1.4 APRA revokes use of the term 'merchant bank'

On 9 February 2012, the Australian Prudential Regulation Authority (APRA) revoked an existing consent for non-regulated financial businesses operating in the short-term money market to describe themselves as 'merchant banks'.

There are 39 non-regulated financial businesses currently entitled to use the term 'merchant bank', although very few of those businesses have actually been using the term.

APRA's decision comes after its review of the guidelines for approval to use the term 'bank' under section 66 of the Banking Act 1959, in response to the Government's 'Competitive and Sustainable Banking System' package announced in December 2010.

For many years the Reserve Bank of Australia and, subsequently, APRA, have allowed money market corporations (listed in Category D of registered financial corporations under the Financial Sector (Collection of Data) Act 2001 ('FSCODA')) to use the restricted word 'bank' only in the expressions 'merchant bank', 'merchant banker' and 'merchant banking'. In its review, APRA found that the term 'merchant bank' had been overtaken in common language by the term 'investment bank', a term that APRA does not allow unauthorized financial businesses to use. Therefore, APRA believes the use of the term 'merchant bank' could cause confusion in the minds of the public when used by entities that are not authorized to carry on banking business in Australia. According to the APRA, the global financial crisis has highlighted the importance of a clear demarcation between the regulated banking system and the non-regulated or 'shadow' financial sector.

APRA has consulted with relevant institutions on its proposal to revoke the existing consent and has provided appropriate transition to allow those businesses using the term 'merchant bank' to revise their promotional material.

Further information on Category D registered financial corporations under FSCODA is available on APRA's website.

Information on guidelines and exemptions relating to section 66 of the Banking Act 1959 can also be found on APRA's website.

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1.5 US Government Accountability Office discussion summary following financial literacy forum

On 9 February 2012, the US Government Accountability Office ('GAO') released a discussion summary following its 20 October 2011 forum on financial literacy.

The forum was convened by GAO to discuss key issues related to financial literacy. Participants included representatives of US federal, state, and local government agencies, academic experts, non-profit practitioners and representatives from the private sector.

'Financial Literacy: Strengthening Partnerships in Challenging Times' summarizes the collective discussion of the forum participants. The following themes were identified during the forum:

the need for financial literacy efforts to focus on key populations and skills;

the need to identify the most effective approaches to improving financial literacy and targeting efforts accordingly;

the need to enhance the role of employers in improving their employees' financial literacy;

the need to leverage the unique role of the federal government in improving financial literacy;

the need to increase coordination and partnerships within and across levels of government and different sectors; and

the need to identify lessons from other initiatives designed to improve consumer behaviours.

The full text of the Forum's discussion summary is available on the GAO website.

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1.6 Government announces closure of the Financial Reporting Panel

On 7 February 2012, the Government announced that the Financial Reporting Panel ('FRP') would be wound up.

The FRP was established in 2006 to resolve contested issues between ASIC and reporting entities over the application of accounting standards to financial reports. According to the Government, the demand on the FRP as an alternative dispute resolution mechanism has proven to be too low to justify its continued operation.

The Government previously announced that it would wind up the FRP in 2010-11 due to lower than expected referral rates. Between 2006, when it was established, and 2010, only one case was referred to the FRP, but the matter was resolved before a determination was made. Four cases were referred to the FRP in August 2010. These referrals led the Government to review whether there was an ongoing role for the FRP but there have been no referrals to the body since that time.

Amendments to the Corporations Act 2001 will be introduced into Parliament to give effect to the Government's decision.

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1.7 UK financial regulation reform: Financial Services Bill introduced in Parliament; White Paper published

On 6 February 2012, the Financial Services Bill received its Second Reading in the UK Parliament, after being introduced in Parliament on 26 January 2012.

The UK Government has also published a White Paper entitled 'A new approach to financial regulation: securing stability, protecting consumers'. The White Paper details the main changes the Government is making to the Financial Services Bill. It includes:

the Government's formal responses to the Joint Committee's report on the earlier draft of the Bill (published on 19 December 2011);

the Treasury Select Committee's report on Bank of England governance and accountability (published November 2011);

a summary of consultation responses received to the White Paper and draft Bill published in June 2011; and

drafts of the memorandums of understanding on crisis management and international organizations which Parliament and stakeholders have asked to see during the course of the Bill's passage.

A copy of the Financial Services Bill is available on the UK Parliament website.

A copy of the White Paper on the Bill is available on the UK Treasury website.

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1.8 COAG Reform Council warns of looming deadline for seamless national economy reforms including nationally consistent approach to the imposition of personal criminal liability on directors

On 3 February 2012, the COAG Reform Council released its third report on the Council of Australian Governments' (COAG) seamless national economy reforms.

The report provides an assessment of the progress of the Commonwealth, States and Territories from 2008-09 to 2010-11. Overall, the report found that 37 reforms have been completed or are on track to be completed by the December 2012 deadline. However, the Reform Council also found that 12 reforms are at risk of not being completed by the deadline.

Once such reform at risk is a nationally consistent approach to the imposition of personal criminal liability on company directors. According to the report, in 2011 the Reform Council was concerned that there had been no process at a multi-jurisdictional level to consider whether the reforms proposed by individual jurisdictions were sufficient. The Reform Council recommended that COAG establish a new process to realize a nationally consistent, principles-based approach to the imposition of personal criminal liability of directors. Despite COAG having set new milestones, the Reform Council remains concerned that the output for this reform may not be achieved on time, based on the poor progress made to date and the fact that the final milestone for this reform only requires jurisdictions to introduce, rather than pass, legislation by December 2012.

In 2008 the Commonwealth, States and Territories agreed to implement regulation and competition reforms under the National Partnership Agreement to Deliver a Seamless National Economy, which now covers 49 separate reforms. The 49 reforms comprise 27 deregulation priorities, 17 areas of competition reform, and reform to regulation making and review processes. In 2009 and 2010, COAG agreed to four additional regulatory reforms. The Reform Council was established by COAG as part of the arrangements for federal financial relations to assist COAG to drive its reform.

On 27 January 2012, the Commonwealth Treasury released for public consultation proposed amendments to Commonwealth directors' liability laws: see Item 1.12 in this Bulletin.

The full text of the COAG report is available on the COAG Reform Council website.

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1.9 CFTC and SEC joint report to Congress on international swap regulation

On 2 February 2012, the US Commodity Futures Trading Commission (CFTC) and the US Securities and Exchange Commission (SEC) delivered to Congress a report on international swap regulation, as required by section 719(c) of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The provision requires the Commissions to report on how swaps are regulated in the United States, Asia, and Europe and to identify areas of regulation that are similar and other areas of regulation that could be harmonized.

The report is available on the CFTC website.

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1.10 BIS seeks views on company law matters

On 2 February 2012, as part of its Red Tape Challenge ('RTC'), the UK Government's Department for Business, Innovation and Skills ('BIS') released a discussion paper which seeks public input on thousands of existing company-related regulations.

The Discussion Paper, titled 'Providing a flexible framework which allows companies to compete and grow', summarizes the views sought on a range of company-related matters, including company names, company filing obligations, the inspection of company registers, penalties and enforcement, and employee share ownership schemes.

The Discussion Paper is available on the BIS website.

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1.11 OECD report on the role of institutional investors in promoting good corporate governance

On 1 February 2012, the OECD released a report titled 'The role of institutional investors in promoting good corporate governance'. The report presents the results of the second thematic peer review based on the OECD Principles of Corporate Governance. It investigates the role of institutional investors in promoting good corporate governance practices, including the incentives they face to promote such outcomes.

The report first presents an overview of the structure and behaviour of institutional investors. It then provides three country reviews of institutional investors in Australia, Chile and Germany. The report covers 26 different jurisdictions, and is based in part on a questionnaire that was sent to all participating jurisdictions in January 2011.

Institutional investors are a major force in many capital markets. According to the report, by 2009 they managed an estimated USD 53 trillion of assets in the OECD area, including USD 22 trillion in equity.

The Report is available on the OECD website.

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1.12 Treasury exposure draft of the Personal Liability for Corporate Fault Reform Bill 2012

On 27 January 2012, Treasury released for public consultation proposed amendments to Commonwealth directors' liability laws. The Personal Liability for Corporate Fault Reform Bill 2012 covers Treasury (non-taxation) legislation. As such, it makes amendments to the Corporations Act 2001, Insurance Contracts Act 1984, Foreign Acquisitions and Takeovers Act 1975 and the Pooled Development Funds Act 1992.

The Bill constitutes the first part of the Commonwealth's implementation of the Council of Australian Governments' (COAG) Directors' Liability reform project. On 29 November 2009, COAG agreed to progress the reforms contained in the National Partnership Agreement to deliver a Seamless National Economy. One of the 27 deregulation priorities is the directors' liability reform project. The project aims to harmonise the imposition of personal criminal liability for corporate fault across Australian jurisdictions.

A second draft bill, encompassing all proposed amendments to Commonwealth legislation will be released in February/March 2012.

The draft Bill is available on the Treasury website.

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1.13 FSA seeks views on proposed amendments to Listing Rules

On 26 January 2012, the UK Financial Services Authority ('FSA') published a Consultation Paper, setting out proposed amendments to the UK Listing Rules, Prospectus Rules, Disclosure Rules and Transparency Rules.

The principal areas in which changes are proposed are:

reverse takeovers;

sponsors;

transactions;

financial information; and

externally managed companies.

The FSA is also seeking public views on some wider issues, including the nature of the premium listing standard and the sufficiency of protections afforded to investors generally.

The Consultation Paper is available on the FSA website.

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1.14 CalSTRS Analysis of 2011 Say-on-Pay Proxy Voting

On 25 January 2012, the California State Teachers' Retirement System (CalSTRS) released 'Lessons Learned: The Inaugural Year of Say-on-Pay', its analysis of shareholders' ability to vote on executive compensation, known as 'say-on-pay', during the 2011 US proxy season.

CalSTRS's report provides key findings from the first year of mandatory say-on-pay for most US corporations. The report notes that some questionable practices are on the decline, such as companies paying taxes on executives' use of perquisites, and excessive perquisites themselves. However, the analysis also discusses CalSTRS's primary reasons for voting against say-on-pay proposals and identifies areas where CalSTRS believes many companies can improve. Among these findings, are:

persistent disconnect between executive pay and company performance was CalSTRS's overwhelming reason for 'against' votes;

continued board use of broad discretion in developing compensation policies remains problematic; and

appropriate peer group selection continues to be a challenge.

Of the 2,166 say-on-pay proposals from the beginning of January through the end of June 2011, CalSTRS voted 'for' nearly 77 percent and 'against' 23 percent of the time. The overwhelming reason for CalSTRS's 'against' votes was the continued disconnect between company performance and executive compensation.

In looking ahead to the 2012 proxy season, the analysis discusses continued challenges investors may face, including the complexity of proxy statements, the use of peer group comparisons as a way to target compensation and the use of total summary compensation tables instead of actual take-home compensation for executives when shareholders consider voting the proxy ballot.

The report is available on the CalSTRS website.

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1.15 World Federation of Exchanges 2011 Market Highlights

On 19 January 2012, the World Federation of Exchanges ('WFE') published its 2011 market highlights.

According to WFE figures, equity volumes in 2011 remained stable despite a fall in market capitalization, while derivatives, bonds, ETFs, and securitized derivatives continued to grow strongly.

Specific 2011 highlights from WFE are as follows:

(i) Equity Markets

A 13.6% decrease brings global equity market capitalization to roughly the same level ($US 47 trillion) as it stood at the end of 2009. Almost all WFE members were affected by the decline, as only four exchange ended 2011 at a higher level. The magnitude of the decline was similar among the three time zones in dollar terms: -15.9% in the Asia-Pacific, -15.2% in EAME, and -10.8% in the Americas.

Despite the market capitalization decline, Electronic Order Book ('EOB') turnover value remained stable at $US 63,080 billion (-0.1%). This figure was heavily influenced by the two largest exchanges by turnover value (NYSE Euronext (US) and NASDAQ OMX US), which represented almost 50% of the total EOB value of share trading.

The number of listings among WFE members increased slightly to 45,953 (+1.7%), in spite of an overall unfavourable macroeconomic environment for primary markets in several regions. The number of EOB trades totalled 112 billion, down 6.4% from the previous year, while the average transaction size was $US 8,700, up 1.8% from the previous year. The latter figure is not surprising given a stable value of share trading and a declining number of trades.

(ii) Derivatives

The number of on-exchange futures and options contracts traded in 2011 increased by 8.9% to 18.5 billion. Increased trading in stock index options and futures and ETF options led the gains, as high volatility and uncertainty over the sovereign debt crisis continued to increase risk management needs.

(iii) Bonds, ETFs and Securitized Derivatives

Bond trading on exchanges increased sharply in 2011, up 35.5% to $US 32.5 trillion, reflecting the growing interest for fixed-income products as well as the security and transparency of the exchange offer.

The 2011 ETF turnover value was $US 10.3 trillion (+7.5%) and the number of listings totalled 6,909 (+24%). The Americas region still dominated this segment (87% of the total volumes), but the two other regions were continuing to catch up with higher growth rates.

Securitized derivatives grew by 51% to 1.1 million, mostly due to a surge in listings in the EAME region where turnover value was also significantly up (+23%). Overall volumes are nearly stable (+2%, $US 1.1 trillion), as the Asia-Pacific region still dominates volume figures (77% of overall total).

The World Federation of Exchanges is the trade association for the operators of regulated financial exchanges. With 54 members from around the globe, the WFE develops and promotes standards in markets, supporting reform in the regulation of OTC derivatives markets, international cooperation and coordination among regulators. WFE exchanges are home to more than 45,000 listed companies.

Further information on WFE annual and monthly statistics is available on the WFE website.

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1.16 BIS seminar papers on Asia Pacific bond markets

In January 2012, the Bank for International Settlements ('BIS') released papers from the jointly organized seminar by the BIS and the Bank of Japan ('BOJ') on 'The development of regional capital markets'. Held in Yokohama, Japan on 21-22 November 2011, the seminar brought together senior officials of 12 central banks in Asia and the Pacific, the European Central Bank, the Bank of Mexico, the Bank of England and the Federal Reserve Bank of New York.

The seminar consisted of five sessions:

1. development of domestic bond markets;

2. development of off-shore bond markets;

3. credit derivatives and structured finance in Asia and the Pacific;

4. credit rating agencies; and

5. market liquidity.

It concluded with a panel discussion on the impact of capital flows on bond market development in Asia.

The seminar papers are available on the BIS website.

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2. Recent ASIC Developments

Next Section

2.1 Policy on enforcement and investigations

On 20 February 2012, ASIC released policy documents discussing how it undertakes investigations and enforcement activity.

The policy documents are:

Information Sheet 151 'ASIC's approach to enforcement' discusses how ASIC approaches enforcement and why it responds to different breaches of the law in different ways.

Information Sheet 152 'Public comment' outlines when ASIC may comment publicly on investigations and enforcement actions. It replaces the public comment policy in Regulatory Guide 47 'Public comment'.

Regulatory Guide 100 'Enforceable undertakings' outlines what an enforceable undertaking (EU) is and when ASIC will consider accepting an enforceable undertaking.

ASIC's decision on whether to take enforcement action is based on assessing:

evidence;

cost vs regulatory benefit; and

level of harm or loss.

The enforceable undertaking guide outlines:

what an enforceable undertaking is;

when ASIC will consider accepting an enforceable undertaking;

what terms are or are not acceptable to ASIC; and

what happens if an enforceable undertaking is not complied with.

To further increase transparency, ASIC shortly plans to publish a report on key enforcement outcomes finalized during the period from 1 July to 31 December 2011. ASIC envisages issuing similar reports bi-annually.

Information Sheet 151, Information Sheet 152 and Regulatory Guide 100 are available on the ASIC website.

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2.2 Policy on indirect self-acquisitions

On 16 February 2012, ASIC released a new regulatory guide outlining the circumstances under which relief will be given to investment funds from the prohibition against indirect self-acquisitions.

Indirect self-acquisition occurs where shares in a company are issued or transferred to an entity it controls. The Corporations Act 2001 voids such an issue or transfer of shares unless certain exceptions apply (refer to section 259C).

Regulatory Guide 233 'Indirect self-acquisition: Relief for investment funds' provides that ASIC may grant conditional relief for investment funds and similar entities to acquire shares in their listed parent company for the benefit of investors. This relief, for example, may assist a subsidiary of a listed company that is also the responsible entity of an investment fund acquiring shares in the listed parent company on behalf of the fund under its investment mandate. ASIC may also grant conditional relief to controlled entities of listed companies engaged in index arbitrage and client-driven activities involving baskets of securities.

The guidance outlines that ASIC's relief will be subject to conditions to address the risks associated with self-acquisitions. For instance, conditions might include a 5% limit on the total interest in a parent company that may be held by its controlled entities (subject to certain limited exclusions) and a prohibition on the voting of such shares. ASIC will also require as a condition of relief regular reporting to the market of a controlled entity's interests in its parent's shares.

ASIC's relief is likely to be used by subsidiaries of a small number of listed companies in the financial services sector who may also be subject to regulation by the Australian Prudential Regulation Authority. ASIC has previously provided relief on a case-by-case basis to these entities and has now finalised its policy after seeking feedback from industry on some issues.

Regulatory Guide 233 is available on the ASIC website.

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2.3 Guidance on financial products and services' advertising

On 14 February 2012, ASIC released guidance to help promoters comply with their legal obligations when advertising financial products and services.

RG 234 'Advertising financial products and advice services: Good practice guidance' builds on ASIC's focus to promote confident and informed investors and financial consumers.

Since July 2010, ASIC's actions have resulted in 117 advertisements across the financial services sector being withdrawn or remedied in response to concerns about poor practices and potentially misleading or deceptive conduct.

ASIC's final guidance on advertising responds to feedback received on Consultation Paper 167 'Advertising financial products and advice services: Good practice guidance'.

Regulatory Guide 234 is available on the ASIC website.

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2.4 Regulatory cooperation arrangement with Canada

On 10 February 2012, ASIC, the Quebec Autorité des marchés financiers ('AMF'), the Ontario Securities Commission ('OSC'), the Alberta Securities Commission ('ASC') and the British Columbia Securities Commission ('BCSC') announced an arrangement to facilitate their supervision of regulated entities that operate both in Australia and Canada.

A memorandum of understanding ('MOU') has been executed that provides a clear mechanism for consultation, cooperation, and exchange of information among ASIC, AMF, OSC, ASC and BCSC in the context of supervision. The MOU sets forth the terms and conditions for the sharing of information about regulated entities, such as broker or dealers, which operate in Australia, Quebec, Ontario, Alberta and British Columbia.

ASIC, AMF, OSC, ASC and BCSC have a long history of cooperation particularly in securities enforcement matters. The MOU extends this cooperation beyond enforcement by setting forth a framework for consultation, cooperation and information-sharing related to the day-to-day supervision and oversight of regulated entities.

The MOU was signed in Tokyo on 10 February 2012, after the close of a meeting of the International Organization of Securities Commissions ('IOSCO'). It is modelled after the principles set out in the IOSCO Task Force on Supervisory Cooperation Report, which was published on 25 May 2010.

In response to the recent financial crisis, the Task Force and many other groups, including the G20, have recommended that regulators enhance the supervision of internationally-active regulated entities by working with their foreign counterparts.

Further information on the MOU is available on the ASIC website.

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2.5 Corporate insolvencies continue to rise over 2011

On 10 February 2012, ASIC released statistics showing that corporate insolvencies rose over the 2011 calendar year, with external administration ('EXAD') appointments increasing 9.2% from the previous year.

Although EXAD appointments had remained relatively steady since the initial increase in activity in 2008 following the global financial crisis, 2011 saw a further rise in appointments, with stronger activity in the June and September quarters, although moderating in the December quarter of 2011.

The number of companies entering into external administration for the past five years is as follows:

2007 - 7,521 (an annual fall of 2.8%)

2008 - 9,113 (an annual rise of 21.2%)

2009 - 9,437 (an annual rise of 3.6%)

2010 - 9,601 (an annual rise of 1.7%)

2011 - 10,481 (an annual rise of 9.2%)

ASIC publishes monthly insolvency statistics detailing the number and type of corporate insolvency appointments. External administrators are obliged by law to notify ASIC of their appointments. ASIC will provide brief commentary on its statistics quarterly throughout the 2011-12 financial year.

Further information on ASIC's insolvency statistics is available on ASIC's website.

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2.6 Warning on secured debt products

On 8 February 2012, ASIC announced measures to help ensure issuers of debt products such as debentures and notes provide investors and financial consumers with the information they need to make informed decisions about investing in these products.

The measures include:

changes to the naming of both listed and unlisted retail debt products to better reflect the nature of the product;

updated regulatory guidance for issuers of unlisted debt products, in particular Regulatory Guide 69 'Debentures and notes: Improving disclosure for retail investors'; and

updated investor information on ASIC's investor and financial consumer website, MoneySmart.

ASIC will now permit issuers of debt to name a product a 'secured note' if there is a first ranked security over some assets, so long as conditions about describing the security are met. Issuers may only call a product a debenture if the security is over tangible property.

All issuers must make clear in their advertising that the products are not a bank deposit and should not suggest that they compare favourably to a bank deposit.

ASIC introduced the 'secured note' description by providing relief to the law under ASIC Class Order 12/1482 'When debentures can be called secured note'. The conditional relief follows the issue in March 2011 of ASIC Consultation Paper 151 'Debt securities: Modifying the naming provisions and advertising requirements'.

Further information is available on ASIC's website.

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2.7 Report on financial market supervision

On 7 February 2012, ASIC issued its third report on the supervision of Australian financial markets and market participants.

Report 277 'ASIC supervision of markets and participants: July to December 2011' identified that during the reporting period:

There were 20,029 trading alerts with 131 matters requiring further consideration during the reporting period.

23 matters were referred for investigation. These matters involved potential insider trading (6), market manipulation (5), possible breaches of the market integrity rules (9) and of the continuous disclosure obligations (3).

A further four matters referred for investigation were identified during ASIC's participant surveillance visits. These related to possible breaches of market integrity rules (2), misleading and deceptive conduct (1), and inappropriate advice (1).

In the reporting period, one case of insider trading and one case of market manipulation were successfully prosecuted, a further three people agreed to plead guilty to insider trading and two companies paid penalties after ASIC issued infringement notices under the Market Integrity Rule regime.

ASIC assumed responsibility for market supervision and real-time surveillance of trading from ASX on 1 August 2010. This now includes supervision of Chi-X Australia, which commenced operations on 31 October 2011. ASIC supervises compliance with market integrity rules, compliance with the Corporations Act 2001 and ensures that Australian financial services license conditions are met by market participants.

Report 277 is available on ASIC's website.

Detailed Contents

2.8 Relief application decisions

On 31 January 2012, ASIC released a report outlining decisions on relief applications between 1 June and 30 September 2011. The report also discusses the various publications released during this period.

The report, 'Overview of decisions on relief applications (June 2011 to September 2011)' ('Report 274') aims to improve the level of transparency and quality of publicly available information about decisions ASIC makes when asked to exercise its discretionary powers to grant relief from provisions of the Corporations Act 2001 ('Corporations Act'), the National Consumer Credit Protection Act 2009 ('National Credit Act') or the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 ('Transitional Act').

ASIC uses its discretion to vary or set aside certain requirements of the law where there is a net regulatory benefit or where ASIC can facilitate business without harming other stakeholders.

Report 274 summarises situations where ASIC has exercised, or refused to exercise, its exemption and modification powers under the Corporations Act, the licensing and responsible lending provisions of the National Credit Act, and the registration provisions of Schedule 2 of the Transitional Act. The report also highlights instances where ASIC has decided to adopt a no-action position regarding specified non-compliance with statutory provisions. Decisions by ASIC to refuse to exercise its powers are described on an anonymous basis.

The report provides examples of decisions that demonstrate how ASIC has applied its policy in practice, which ASIC thinks will be of particular interest to capital market participants and those working in the consumer credit and financial services industries. The report includes an appendix detailing the relief instruments ASIC executed.

Report 274 is available on ASIC's website.

Detailed Contents

2.9 Guidance for agribusiness managed investor schemes

On 30 January 2012, ASIC released an investor guide and regulatory guidance with new disclosure benchmarks and principles for agribusiness managed investment schemes to improve investor awareness of the risks associated with these products.

These risks have been highlighted since 2008 when several operators of agribusiness schemes failed, causing investors significant losses. The collapses highlighted features of agribusiness schemes and raised concerns about whether these features and associated risks were adequately disclosed to investors.

Regulatory Guide 232 'Agribusiness managed investment schemes: Improving disclosure for retail investors' outlines five benchmarks and five disclosure principles that apply to all agribusiness schemes. Agribusiness schemes must disclose whether they meet the benchmarks and if not, why not. 'Why not' means explaining how they will deal with the business factor or the issue underlying the benchmark.

RG 232 is the latest in the series of 'if not, why not' disclosure benchmarks for sectors that pose particular risk to investors and financial consumers. It follows the issue of disclosure benchmarks for the infrastructure and over-the-counter contracts for difference sectors in Regulatory Guide 231 'Infrastructure entities: improving disclosure for retail investors' and Regulatory Guide 227 'Over-the-counter contracts for difference: Improving disclosure for retail investors'.

Agribusiness schemes pose particular risks because unlike many other types of managed investment schemes, they do not generally use a traditional unit trust structure. For tax reasons, many agribusiness schemes are structured so that investors operate their agribusiness investment in their own right. Investors enter into contracts with the responsible entity or other parties to perform all the cultivation and management activities associated with the investor's agribusiness enterprise. Investors need to understand these complex arrangements as an investment in an agribusiness scheme is a long-term commitment and investors may have ongoing obligations in relation to the operation of their agribusiness enterprise.

RG 232 also outlines the standards ASIC expects responsible entities to meet when advertising agribusiness schemes to retail investors and guidance as to clear, concise and effective disclosure of the benchmark and disclosure principle information.

Responsible entities of agribusiness schemes should disclose the benchmark and disclosure principle information in any product disclosure statement dated on or after 1 August 2012.

Regulatory Guide 232 and ASIC's Agribusiness investor guide are available on ASIC's website.

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3. Recent ASX Developments

Next Section

3.1 Equity Exchange Traded Options (ETOs) Market Structure Reform Proposals

On 17 January 2012, ASX released a consultation paper 'Equity Exchange Traded Options (ETOs) Market - Market Structure Reform Proposals 2012-2014'. The consultation paper sets out discussion points on the next set of reforms and developments ASX should consider undertaking for the ETO Market.

In 2009, ASX began work on a series of ETO Market and Product development reforms and further reforms are scheduled to be implemented within the next 15 months. These reforms are listed in the consultation paper.

ASX is now commencing the consultation phase for the next set of reforms and developments beyond those noted in the consultation paper. This consultation paper seeks market views on aspects of the current ETO market structure, including:

ETO crossing rules and procedures

Display of Participant Codes

Exercise and assignment allocation process

Corporate actions creating basket options

Differentiated ETO registration fees.

ASX welcomes comments from interested stakeholders by 28 March 2012. ASX invites market makers, brokers, institutional users, retail users and clearers to suggest, in detail, reasoned arguments supporting their views on the above topics and any other reform or development policy topics.

A copy of the consultation paper is available on ASXGroup.com.au.

Detailed Contents

3.2 Reports

On 3 February 2012, ASX released:

the ASX Group Monthly Activity Report;

the ASX 24 Monthly Volume and Open Interest Report; and

the ASX Compliance Monthly Activity Report

for January 2012.

Detailed Contents

4. Recent Corporate Law Decisions

Next Section

4.1 Affidavit in support of winding-up application valid

(By William Thomas, Blake Dawson)

Deputy Commissioner of Taxation v National Skin Institute (Aust) Pty Ltd [2012] FCAFC 2, Federal Court of Australia, Full Court, Finn, Gordon and Murphy JJ, 2 February 2012

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/cth/FCAFC/2012/2.html

(a) Summary

The Full Court of the Federal Court held that an affidavit sworn by an officer of the Deputy Commissioner of Taxation ('the Commissioner') in support of an application to wind up National Skin Institute (Aust) Pty Ltd ('the Company') complied with the requirements set out at section 459Q of the Corporations Act 2001 (Cth) ('the Act').

(b) Facts

The Commissioner served a creditor's statutory demand for payment of a debt of $400,590.50 on the Company. The Company did not respond to the statutory demand. As a result, the Commissioner brought an application to wind up the Company in insolvency under section 459P of the Act.

The application was supported by an affidavit, as required under section 459P. The affidavit was validly sworn by an officer of the Commissioner. The issue in this case concerned the admissibility of three paragraphs in the affidavit. Since the affidavit was in a standard form which the Commissioner had used in winding up applications for many years, the issue was considered to be of general application justifying referral to the Full Court.

The disputed paragraphs of the affidavit provided that:

The facts contained within the affidavit were within the personal knowledge of the Commissioner's officer and drawn from information possessed by the ATO to which the officer had access. This paragraph was disputed because it did not state the particular information which the officer has accessed.

The Company owed $400,590.50 to the Commonwealth. This paragraph was disputed because it was a mere assertion and did not state the source of the officer's knowledge.

The Company had not yet paid the debt. This paragraph was disputed for the same reason as the paragraph above.

It was submitted on behalf of the Company that these paragraphs did not conform to the requirements set out in section 459Q of the Act. In particular, it was submitted that the affidavit failed to verify that the debt was due and payable by the Company, contrary to section 459Q(c)(ii) of the Act. Further, it was submitted that the paragraphs were inadmissible as they infringed the hearsay rule in section 59 of the Evidence Act 1995 (Cth).

(c) Decision

The decision focused on the meaning of the word "verify" in section 459Q. The Court found that "verify" was language of "a formal affirmation" that did not require additional material to be adduced to prove the existence of the debt. Therefore, the affidavit was not incomplete contrary to section 459Q.

The legislative context supported this interpretation. In particular, the Act contained a rebuttable presumption that where a company failed to respond to a statutory demand within 21 days, it would bear the burden of proving that it was solvent when the winding up application was heard. The Company had not at any time sought to rebut the presumption that it was insolvent.

The purpose of the affidavit was therefore merely to confirm, rather than prove, that the debt was still payable. In this case, it was sufficient that the affidavit referred to the officer's personal knowledge and information possessed by the ATO in order to confirm the existence of the debt.

The Court supported its decision with several further points:

The Court had the power under section 467A of the Act to grant a winding up application even if it was not made in conformity with section 459Q, as long as the company which was the subject of the application had not suffered substantial injustice. This provision indicated that non-compliance would not necessarily lead to dismissal of the application.

The hearing was unopposed. This meant that the Court was entitled to consider evidence to which the Company may have objected, as long as it was not prohibited by an absolute rule at law.

The affidavit was not in dissimilar terms to the example contained in a schedule to the Federal Court (Corporations) Rules 2000 (Cth).

The Court ordered that the Company be wound up in insolvency.

Detailed Contents

4.2 Dealing with company property by directors

(By John O'Grady and Daniel Davids, Corrs Chambers Westgarth)

GHLM Trading Limited v Anil Kumar Maroo [2012] EWHC 61 (Ch), England and Wales High Court (Chancery Division), Newey J, 23 January 2012

The full text of this judgment is available at:

http://www.bailii.org/ew/cases/EWHC/Ch/2012/61.html

(a) Summary

The case centred around various allegations by GHLM Trading Limited ('GHLM') (a clothing company) against Anil Kumar Maroo and Nita Anilkumari Maroo (the 'Maroos'), the first and second defendants and the only directors of GHLM at the time.

The key allegations were that the Maroos had falsified numerous credit entries on the directors' loan account ('DLA'). GHLM argued that the Maroos' position as directors meant that they bore the burden of proof, as fiduciaries of the company, to account for all entries made to the DLA.

Newey J accepted this proposition and stated that the close analogy between directors and trustees meant that, just as trustees had to account for trust property, so too did directors have to account for company property.

After detailed cross-examination of the Maroos, Newey J held that approximately half of the credited amounts on the DLA were unjustified and that Mr Maroo had falsified numerous financial accounts and records of GHLM in order to try and explain those unjustified credited amounts.

The other main issue disputed between the parties involved a claim that the Maroos had breached their directors' duty to GHLM to, in good faith, promote the success of the company per section 172 of the Companies Act (UK) 2006. His Honour found a breach of the duty in section 172 for the following two reasons:

1. the Maroos sold GHLM's trading stock to Brocade International Limited ('Brocade'), the third defendant and a company of which the Maroos were the sole directors and shareholders, at a time when they knew the company to be verging on insolvency; and

2. the Maroos failed to disclose their wrongdoings to GHLM's sole shareholder, Shildon Holdings Limited ('Shildon').

(b) Facts

The Maroos were the directors of GHLM (a clothing company) and all issued shares in GHLM were held by Mrs Maroo. In February 2005, Mr Maroo and Braj Binani entered into an agreement whereby Shildon, a company of which Mr Binani was the ultimate beneficial owner, became GHLM's sole shareholder by acquiring all of Mrs Maroo's shares in exchange for £1 million. However, the Maroos stayed on as directors of GHLM and were paid remuneration in the form of consultancy fees to Brocade.

GHLM carried on its business in collaboration with several textile companies (including Brocade), as well as clothing stores through which GHLM could distribute trading stock. Most of these stores were owned and managed by the Maroos.

During the period of 2005-2007, Mr Binani made several substantial loans to GHLM at the request of Mr Maroo in addition to his initial £1 million equity investment. Over the same period, Mr Maroo was found to have knowingly misled Mr Binani to make it look like loan money was being used within GHLM when it was likely being used for Mr Maroo's own purposes.

In 2005, GHLM was experiencing cash-flow problems and it is likely that Mr Maroo was aware that the business was nearing insolvency at this stage. By May 2007, Mr Binani decided that GHLM should be wound up and hired Vimal Shah to oversee the winding-down of GHLM's affairs.

Mr Maroo employed delay tactics throughout 2007-2009 in a bid to prevent Mr Shah's access to company accounts. During this period Mr Maroo also engaged in a number of fraudulent practices involving the accounts, financial records and contracts of the company in order to cover up numerous misuses of company money and to cover up falsely credited amounts that had been made to the DLA.

On 31 March 2008, Mr Shah informed Mr Maroo that his services would come to an end on 30 April 2008. However, Mr Maroo said he would not step down unless paid £100,000, an amount which was claimed to be part of the original consideration for the purchase of the business, as well as being allowed to take £150,000 worth of trading stock in repayment of a loan which Mr Maroo had allegedly made to GHLM.

On 01 June 2008, Mr Shah again requested that the Maroos resign as directors. Mr Maroo replied that he and Mrs Maroo would resign that month. However, no such resignation occurred, and in October 2008 Mr Maroo sent an email to Mr Binani stating that settlement would need to be reached before the Maroos would resign.

On 4 December 2008, the Maroos passed a directors' resolution to sell GHLM's trading stock to Brocade on the basis that the purchase price would be set off against sums said to be due and owing to Brocade.

On 10 December 2008, Shildon requested that a general meeting of GHLM be called so that resolutions could be passed removing the Maroos as directors of GHLM. Mr Maroo responded with further delay tactics by claiming that the notice was insufficient per statutory requirements, and that as he was out of the country he would deal with the issue upon his return to the UK in early January 2009.

On 5 January 2009, a general meeting of GHLM was purportedly held where three directors were appointed who then held a board meeting at which they immediately suspended the Maroos as directors of GHLM. However, Mr Maroo continued to undertake management of the company (including the sale of GHLM's trading stock to Brocade) while refusing to meet with Mr Shah or other representatives of Mr Binani under the false pretense that he was out of the country and unavailable.

On 25 January 2009 Mr Maroo, without informing GHLM's newly appointed directors, purported to remove them from the board.

The Maroos were definitively removed as directors of GHLM at a general meeting held on 11 March 2009.

(c) Decision

(i) The director's burden as a fiduciary to account for company property

The largest of the GHLM's claims concerned the Maroos use of the DLA. While the Maroos were directors of GHLM, extensive use was made of their loan account. GHLM challenged many of the credit entries in the DLA, whilst the Maroos contended that they were justified.

GHLM argued that the Maroos' position as directors meant that they bore the burden of proof, as fiduciaries of the company, to account for all entries made to the DLA.

In deciding whether there was an onus on directors to account for company property, Newey J considered the fiduciary duties owed by a trustee to account for trust property and whether such a duty was able to be transposed to a director in relation to company property. Relying on Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd [2011] EWCA Civ 347, Newey J found that 'the close analogy between directors and trustee suggests...that, much as a trustee must show what he has done with trust property, it is incumbent on a director to explain what has become of company property in his hands.'

On the basis of this finding, Newey J agreed with GHLM that, once it is shown that a company director has received company money, it is for that director to show that the payment was proper. Similarly it was accepted that, where debit entries have correctly been made to a DLA, it must be incumbent on the director to justify credit entries on the DLA. Newey J considered this an especially pertinent burden for directors as a director is the person responsible for the management of the company's business and it is a director who has responsibility for ensuring that proper accounting records have been kept.

On the facts, Mr Maroo's explanation for £773,935 of the £1,341,163 credited on the DLA could not be justified and so was held to be owing to GHLM.

(ii) Director must consider the interests of the creditors as a class where the company is insolvent or nearing insolvency

Under section 172 of the Companies Act (UK) 2006, a director must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. However, the interests of the creditors as a class may intrude as the relevant interests to be considered under section 172 when the company is insolvent or nearing insolvency.

As it was established on evidence that Mr Maroo was aware that the company was insolvent (or on the verge of insolvency) by January 2008 at the latest, the Maroos needed to have regard to the company's creditors as a class at that time.

Accordingly, the Maroos when contracting to sell GHLM's trading stock to Brocade were required to have regard to the company's creditors as a class. However, while Mr Maroo claimed that the transaction was in consideration of a debt claimed to be owed to Brocade, Newey J held that it was clear that the transaction was undertaken with a view to the personal interests of the Maroos only (as potential creditors), rather than as a transaction undertaken in the collective interests of GHLM's creditors as a class (or even the interests of GHLM itself or GHLM's members).

Furthermore, the contract with Brocade was found to be void as (a) it was entered into for the personal interests of the Maroos, and (b) the contracting party, Brocade, could be said to have had notice of such a purpose given the Maroos' relationship to Brocade (ie as Brocade's only directors and shareholders).

(iii) The requirement for directors to disclose wrongdoings under the duty to promote the success of the company

GHLM contended that the Maroos, in breach of their fiduciary duties, failed to disclose wrongdoing.

Newey J accepted Arden LJ's statement in Item Software (UK) Ltd v Fassihi [2004] EWCA Civ 1244 that a director's fundamental duty to act in good faith and in the best interests of the company could mean that a director has to disclose their own misconduct. However, Newey J limited the application of this principle by stating that 'a company complaining of a director's failure to disclose misconduct must...establish that the fiduciary subjectively concluded that disclosure was in the company's interests or, at least, that the director would have so concluded had he been acting in good faith.'

The issue of to whom disclosure should be made was less clear. Newey J commented that while disclosure to the board would normally suffice, it was possible for a director to be bound to disclose a matter to someone other than their fellow board members. As the duty of the director is to act in the best interests of the company, it was held that, if a director subjectively concluded that it was in the company's best interests for a matter to be disclosed to a person who was not a member of the board, such disclosure to that other party would need to be made. However, Newey J warned that the duty is owed to the company such that it is the company's interests, and not the shareholder's interests, which will need to be considered by the director.

Newey J concluded that, while the duty may potentially require a director to disclose misconduct in some circumstances, this must be argued on the facts and GHLM was found to have not properly made out such a case. Furthermore, Newey J found it doubtful that disclosure would have led to the earlier termination of the Maroos as Mr Binani had not been able to remove the Maroos as directors of GHLM until well after the date that he first signified such an intention to do so.

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4.3 Canadian Supreme Court finds proposed Canada Securities Act unconstitutional

(By Nigel Campbell and Doug McLeod, Blake, Cassels & Graydon (Canada))

Reference re Securities Act, 2011 SCC 66, Supreme Court of Canada, McLachlin CJ, Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein and Cromwell JJ, 22 December 2011

The full text of this judgment is available at:

http://scc.lexum.org/en/2011/2011scc66/2011scc66.html

(a) Summary

The Supreme Court of Canada has rendered a unanimous decision that the proposed Canada Securities Act ('the Proposed Act') is not constitutional. In doing so, the Court has defeated the Canadian federal government's initiative to establish a single national securities regulator.

The decision comes in response to a reference directed by the Government of Canada on the question of whether the Proposed Act was constitutional. Arguments on the reference were heard earlier in 2011, as were two similar references directed by the provinces of Quebec and Alberta to their respective appellate courts.

(b) Facts

The reference turned on whether the federal government was authorized to regulate securities pursuant to its power over matters of "trade and commerce". This question raised two overarching issues. First, did the "nature" of trading in securities bring it within the scope of the "trade and commerce" power? And second, what would be the constitutional implications of recognizing such a federal power?

(i) Nature of "Trading in Securities"

A series of Supreme Court precedents has established that the test for whether a given matter will fall within the federal "trade and commerce" power will depend, in essence, on whether that matter is of a "general" nature, such that it cannot be adequately regulated at the provincial level - regulation of competition is one example of such a matter. Accordingly, the first major issue before the Supreme Court in the reference on the Proposed Act was whether the regulation of securities involves simply the regulation of a series of purchase and sale contracts pertaining to property - in which case, it would fall solely within the provincial power over "property and civil rights" - or whether it also has a broader aspect that properly brings it within the concurrent jurisdiction of the federal government.

(ii) Constitutional Precedent Created

Over the course of the reference hearings, it became clear that the justices of the Supreme Court were also very mindful of the broader constitutional precedent they would be creating by recognizing federal power over securities.

On the one hand, as pointed out by proponents of the Proposed Act, recognizing a concurrent federal jurisdiction over the regulation of securities would have no immediate impact on the long-recognized provincial power over securities regulation, nor over the legitimacy of the provincial Securities Acts. This point was underscored by the fact that the Proposed Act expressly contemplates a voluntary opt-in scheme by which provinces would be given the choice of whether to opt-in to the proposed federal regulator or to retain their provincial regimes.

However, once recognized, a federal power over securities regulation could apply to empower the federal government not only with respect to the Proposed Act but with respect to future legislation as well, including any future legislation compelling the provinces to comply with a federal regime at the expense of their provincial legislation. As such, by recognizing a concurrent federal jurisdiction, the Supreme Court would be potentially opening the door to significant reorientation of the division of powers. It was these concerns that led to sharp opposition to the federal government's reference on the part of some of the provinces.

(c) Decision

The Supreme Court's unanimous decision was premised on its finding that the "main thrust" of the Proposed Act, which it found to be the "day-to-day" regulation of securities, was not qualitatively different from the regulation already undertaken at the provincial level. On that basis, the Court found that the Proposed Act did not contemplate a distinct matter of genuinely national or general scope as would be required for it to fall within the ambit of the "trade and commerce" power. Echoing the concerns expressed by many of the justices at the reference hearings, the Court found that interpreting "trade and commerce" so broadly as to encompass matters of day-to-day regulation of securities contracts would deny the provinces their proper authority over "property and civil rights", and as such, would upset the balance of federalism.

Notably, the Supreme Court did recognize that certain aspects of securities regulation would likely fall within federal jurisdiction. In particular, the federal government would likely have the authority to regulate aspects of securities bearing upon systemic risk and the preservation of capital markets stability. However, the Court found that regulating these aspects did not require also regulating the "day-to-day" aspects of securities regulation that was the focus of the Proposed Act. Therefore, the Proposed Act could not be saved by the aspects of securities regulation falling within federal jurisdiction.

(d) Where to from here?

The Supreme Court's decision, and the lack of any dissent or disagreement amongst the Court, constitutes a serious, if not fatal, blow to the prospect of comprehensive federal regulation of securities in Canada.

That said, while the Supreme Court's decision likely spells the end of the federal government's current effort to create a comprehensive national regulatory regime, it is possible that a more targeted federal effort could yet be successful, and the national Transition Office established by the federal government as part of its initiative will no doubt be reviewing the Court's decision closely. As noted, the Court has indicated that the federal government has authority over some of the more systemic aspects of securities regulation, and it may be possible that a narrower federal initiative to regulate those aspects, possibly premised on the consent and co-operation of some or all of the provinces, could yet be pursued. Notably, the Court made a point of stating in its decision that such a co-operative effort would be constitutionally legitimate.

Nonetheless, taken overall, it appears more certain than ever that Canada's patchwork of provincial securities regulations is here to stay.

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4.4 Enforcement of indemnity

(By Sarah Horan, DLA Piper)

Paterson v Pongrass Group Operations Pty Ltd [2011] NSWSC 1588, Supreme Court of New South Wales, White J, 20 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/nsw/NSWSC/2011/1588.html

(a) Summary

In this case, White J considered a claim to enforce an indemnity given by the defendant, Pongrass Group Operations Pty Ltd ('PGO') to the plaintiff, John Paterson ('Paterson'), against his liability to penalties incurred to the Australian Tax Office ('ATO') as a director of four subsidiaries of PGO.

The key issues in dispute were:

whether the court should refuse its aid to the enforcement of the indemnity because the indemnity was an outcome of an agreement between Paterson and Pongrass to attempt to obtain financial advantage by deception;

if the indemnity was enforceable, whether it merely required PGO to pay Paterson amounts for which he was liable after he paid the ATO, or whether it required PGO to relieve Paterson by preventing his having to pay the penalties for which he was liable;

if the latter, whether Paterson's action was an action at law for damages or in equity for specific performance or other equitable relief;

if the indemnity was only to compensate Paterson against penalties paid by him, whether he was nonetheless entitled to quia timet relief in equity;

in so far as Paterson sought equitable relief, whether valuable consideration was provided for the indemnity; and

to what relief was Paterson entitled.

White J upheld the indemnity and ordered that PGO relieve Paterson of the full burden of his liability.

(b) Facts

PGO was the holding company of two groups of subsidiaries referred to as the Wilcom Group and the Arcade Group. Robert Pongrass ('Pongrass') was the sole director of PGO. Adrian Crouch ('Crouch') was the chief financial officer of PGO and was a director of a number of subsidiaries of the PGO group, including Wilcom International, Arcade Embroidery and Embroidery Machinery, until he resigned on 17 January 2003.

On or about 17 January 2003, Paterson was appointed as the sole director of 17 of the subsidiary companies of the PGO group, a number of which had significant tax debts, including Wilcom International, Arcade Embroidery, Embroidery Machinery and Initial ('the subsidiaries'). Paterson's role as director was to place PGO subsidiaries into voluntary administration at the direction of Pongrass and Crouch. It is clear from correspondence between Paterson and Pongrass that it was Pongrass' intention that Paterson, who had no significant assets, be appointed as a 'straw man' to provide 'asset protection'.

Between 2003 and 2005, Pongrass received a number of director penalty notices from the ATO in respect of taxes owed by the subsidiaries. The notices stated that Paterson was liable to pay a penalty in an amount equal to the unpaid amount of each liability of those companies in respect of PAYG Witholding Amounts that had not been remitted. Crouch told Paterson that a solicitor engaged to act on behalf of PGO and its subsidiaries was negotiating payment arrangements with the ATO and he instructed Paterson to send his notices to him.

On 10 April 2005, Paterson was served with a statement of claim in which he was named as a defendant, in which the ATO sought to recover $650,874.28 against him personally. Whilst Pongrass told Paterson that PGO would pay any legal fees required to defend his position (and Paterson was satisfied that this particular claim could be satisfactorily defended), Paterson sought an indemnity from PGO against liabilities he had incurred as a result of taking office as a director of the subsidiaries.

A deed of indemnity between Paterson and PGO was duly executed. Recital 2 of the deed of indemnity provided: "The indemnified is prepared to be a director of such corporations providing only that an indemnity is provided to him in the terms of this deed."

Paterson deposed that Pongrass also proposed that, in order to eliminate Paterson's exposure to future liabilities, Paterson resign from all PGO companies, except for one subsidiary, Venture Corp. Paterson undertook to comply with Pongrass' proposal and agreed to cooperate with PGO in its negotiations with the ATO on the proviso that he was given the deed of indemnity.

On 11 October 2010, the Deputy Commissioner of Taxation served a payment demand on Paterson for an amount of close to $2 million and advised that the ATO was considering legal action for the recovery of that amount. Paterson issued proceedings in the Supreme Court of New South Wales to enforce the indemnity given to him by PGO against his liability to penalties incurred as a director of the subsidiaries. He sought damages for breach of the indemnity for the full amount he was liable to pay the ATO.

PGO denied that it was liable to pay any moneys under the indemnity because Paterson had not paid any part of the penalties incurred. It also asserted that there was no consideration (apart from its seal to the deed) for its promise of indemnity, its promise of indemnity was purely voluntary and that equity would not assist Paterson as a volunteer.

(c) Decision

(i) Public policy

The court considered whether the enforcement of the deed of indemnity should be refused on the grounds of illegality, namely obtaining financial advantage by deception.

White J found that Pongrass and Paterson had conspired to attempt to obtain a financial advantage for Pongrass and other directors of the subsidiaries, by deceiving those who would be appointed as voluntary administrators as to the identity of the true directors. The deed of indemnity was an outcome of that deception. However, the indemnity itself was not the deception.

Accordingly, whilst his Honour noted that the court would not lend its aid to a plaintiff who found a cause of action upon an illegal act, particularly where both parties are equally in fault, in light of the fact that Paterson's cause of action was grounded upon the deed of indemnity, which was not itself part of the intended deception, it would be in the public interest to enforce the deed of indemnity.

(ii) Nature of the indemnity

In reaching his determination with respect to the nature of the indemnity, White J observed that the proper construction of any contract of indemnity must depend on the terms of the individual contract, considered in the objective matrix of the facts in which the contract was entered into.

Distinguishing the High Court's decision in Wren v Mahoney [1972] HCA 47, his Honour held that the wording of the deed of indemnity, supported by its factual context, provided both a promise to prevent Paterson from suffering loss arising out of a described claim and a promise to compensate him in respect of any such loss. As such, the indemnity required PGO to relieve Paterson by preventing his having to pay the penalties for which he was liable (rather than purely compensating him for any amounts of penalties that he paid to the ATO).

(iii) Damages or equitable relief

White J held that damages were not an adequate remedy in this case. His Honour noted that there was no reason in principle why substantial damages should not be payable in the event of a breach of an indemnity to prevent a plaintiff from suffering loss, as distinct from compensating a plaintiff for moneys paid by him. However, in this instance, if Paterson was awarded damages for the amount of the liability and the ATO never sought to enforce the liability (which had been outstanding for eight years), Paterson would be overcompensated. As an assessment of damages would have to take into account the contingency that the ATO may never enforce the liability, such an assessment would be uncertain.

Accordingly, White J held that damages would fall for assessment only if equitable relief by way of specific enforcement was not available.

(iv) Quia timet relief

Given that White J had determined that the deed of indemnity not only required PGO to compensate Paterson for penalties paid by him, but also to relieve him of the burden of the liability, the issue of quia timet relief did not fall for consideration.

However, his Honour observed that if PGO's only obligation under an express contract of indemnity had been to indemnify Paterson against amounts already paid, he would not have been entitled to equitable quia timet relief.

(v) Consideration for the promise of indemnity

White J held that Recital 2 to the deed of indemnity stated sufficient consideration for the promise of indemnity, namely Paterson's agreement to continue as director of the subsidiaries, notwithstanding that the recital was 'incorrect' (Paterson did not continue as a director of the subsidiaries). His Honour observed that a party cannot deny that it provided consideration for its promise in a deed, where the deed states that consideration was given and where the question arises in an action brought on the deed.

Further, his Honour concluded that even if PGO was not bound by the recital, consideration was provided by an implied promise on the part of Paterson, which was so obvious as to go without saying, to continue to provide his cooperation in negotiations with the ATO.

Accordingly, White J held that Paterson was entitled to remedies in equity as well as at law on the action to enforce the deed.

(vi) Appropriate remedy

Having considered various forms of equitable relief, White J ultimately ordered that PGO pay Paterson the total liability on Paterson's undertaking to the court to apply the payment forthwith in discharge of his liability to the ATO. As his Honour observed, citing Harvey CJ in McIntosh v Dalwood (No 3) (1930) 30 SR NSW 332, equity is a more satisfactory and proper remedy to make available to the plaintiff than requiring him to sustain the loss and then seek such damages at law as he is entitled to under his contract.

Detailed Contents

4.5 Dishonest diversion of business opportunity a breach of fiduciary and statutory duty

(By Cait Storr, Freehills)

Omnilab Media Pty Ltd v Digital Cinema Network Pty Ltd [2011] FCAFC 166, Federal Court of Australia, Full Court, Jacobson, Rares and Besanko JJ, 19 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/cth/FCAFC/2011/166.html

(a) Summary

Appeals against the decision of primary judge Gordon J were dismissed, upholding her finding of dishonest and fraudulent breach of the fiduciary duty owed by Mr Smith to Digital Camera Network Pty Ltd ('DCN'), with the knowing assistance of Omnilab Media Pty Ltd ('Omnilab').

Holding himself out as a representative of DCN, Mr Smith conducted negotiations with American film studios in order to secure a lucrative position as deployment entity in the industry-wide conversion of movie projection in independent Australian cinemas from analogue to digital. At around the same time, and holding himself out as a representative of his own company MGS Pty Ltd ('MGS'), Mr Smith approached the peak industry body for independent cinemas, the ICAA, which informed him that it was considering appointing a different company, Omnilab, as its deployment entity. Mr Smith subsequently provided business information, including draft VPF agreements naming DCN as the deployment entity, to Omnilab.

DCN brought claims against Mr Smith for breach of his fiduciary and statutory duties to DCN as director, and claims against Omnilab of knowing assistance and accessory liability. The primary judge, via a lengthy summary of the facts, held in favour of DCN on all counts.

Jacobson, Rares and Besanko JJ affirmed the primary judge's decision, holding that:

the facts clearly disclosed that Mr Smith had breached the business opportunity and conflict rules that founded his fiduciary duty to DCN, and in so doing had contravened sections 181(1), 182(1) and/or 183(1) of the Corporations Act 2001 (Cth);

although the dishonesty of Mr Smith's breach was not as clearly evidenced on the facts, it had nonetheless been open to the primary judge to conclude that Mr Smith's breach had been dishonest; and

it had similarly been open to the primary judge to conclude that Omnilab had knowingly assisted in Mr Smith's breach of his fiduciary duty with actual knowledge, rather than with a lesser category of knowledge as argued on appeal by Omnilab; and that this contravened section 179 of the Corporations Act.

(b) Facts

DCN was a joint venture company formed in about July 2008 for the purpose of exploiting business opportunities in the conversion of movie projection from analogue to digital. These business opportunities are lucrative, and include the sale of digital conversion equipment by major American film studios to Australian independent cinema owners. As an incentive to purchase the expensive equipment, the American studios were offering to subsidise purchase via 'Virtual Print Fee' ('VPF') agreements, but were not open to negotiating individual agreements with individual operators, preferring instead to settle a single agreement with a 'digital integrator' or deployment entity able to represent a sufficient number of operators to make an agreement worthwhile to the studios.

DCN consisted of two companies, Smith's company MGS, and digitAll Pty Ltd, a company controlled by the Gardiner brothers. Mr Smith began approaching American studios in October 2008 to negotiate a VPF agreement, holding himself out as a representative of DCN. He further represented to the studios that he enjoyed the support of the ICAA. However, in his dealings with the ICAA, Mr Smith held himself out as a representative of MGS, his own company.

ICAA made clear to Mr Smith that it was considering appointing a different company, Omnilab Media Pty Ltd (Omnilab), to act as its deployment entity in any VPF agreement with the American studios. Mr Smith subsequently provided to Omnilab copies of partly negotiated VPF agreements in which DCN was named as the deployment entity.

(c) Decision

(i) Scope and breach of fiduciary duty

Jacobson J provided the lead judgment in the decision, with Rares and Besanko JJ in agreement. His Honour upheld the primary judge's finding that Mr Smith had breached his fiduciary duty to DCN, finding as follows:

the scope of the fiduciary duty must be moulded according to the nature of the particular relationship and the facts of the case (Hospital Products Ltd v United States Surgical Corporation (1984) 156 CLR at 69 and 102); and in Mr Smith's case, the subject of his duties to DCN was the corporate opportunity he obtained in his capacity as a director of DCN during the negotiations he conducted with the American studios for the VPF agreements;

in providing information including draft VPF agreements to Omnilab without the consent of DCN, Mr Smith had therefore breached the business opportunity rule, which 'disqualifies a director from usurping for himself or diverting to another person..a maturing business opportunity which his company is actually pursuing' (Canadian Aero Service Ltd v O'Malley [1974] SCR 592 at 607); and

in holding himself out at certain times as negotiating on behalf of DCN, and at other times on behalf of MGS, Mr Smith had breached the conflict rule by allowing a conflict or possible conflict to emerge between his fiduciary duty and his personal interest (Chan v Zachariah (1984) 154 CLR 178 at 198).

(ii) Accessorial liability / knowing assistance in a dishonest and fraudulent design

In upholding the primary judge's finding that Omnilab had knowingly assisted in a dishonest and fraudulent design, Jacobson J reiterated that any breach of fiduciary duty relied upon to support a claim of accessorial liability under the second limb of Barnes v Addy must be dishonest and fraudulent (Farah Constructions Pty Ltd v Say-Dee Pty Ltd (2007) 230 CLR 89); but that a person may have acted dishonestly by the standards of ordinary and decent people without appreciating that the act in question was dishonest (Farah v Say-Dee). After raising concern as to whether the evidence necessarily disclosed that Mr Smith's breach was dishonest and fraudulent, his Honour affirmed that the primary judge's finding that Mr Smith had failed to make full disclosure of the assistance he had provided to Omnilab to his joint venturers in DCN provided a sufficient basis for a finding of dishonesty.

Jacobson J upheld the finding that Omnilab's knowledge was actual knowledge as defined by the first of the Baden categories, dismissing Omnilab's claim on appeal that its knowledge was properly characterised as of the second to fourth Baden category (Baden v Societe Generale SA [1993] 1 WLR 509).

His Honour affirmed the primary judge's conclusion on the facts that Omnilab (via a general manager, Mr John Fleming) had actual knowledge that Mr Smith was negotiating the VPF agreements with the American studios on behalf of DCN and not MGS, and that he was providing information to Omnilab without the consent of the Gardiner brothers.

(iii) Procedural fairness

Jacobson J noted that the case had proceeded as a Fast Track matter, with Fast Track statements given in place of full pleadings and particulars; and that this enlivened the warning given in the authorities that claims of dishonesty and of knowing participation in a dishonest and fraudulent design must be properly pleaded and particularised (Farah v Say-Dee). His Honour held that, although DCN's Fast Track statement could have been drafted with more precision, the 'gravamen' of the claim of diversion of DCN's business fell within the terms of their statement, and the primary judge's characterisation of the claim as one of knowing assistance was therefore sufficiently founded.

Detailed Contents

4.6 Privilege not waived in board minutes and advice requested to be produced under section 247A

(By Andrew Westcott, Clayton Utz)

Hanks v Admiralty Resources NL (No 2) [2011] FCA 1464, Federal Court of Australia, Gordon J, 16 December 2011

The full text of the judgment is available at:

http://www.austlii.edu.au/cgi-bin/sinodisp/au/cases/cth/FCA/2011/1464.html

(a) Summary

This decision of the Federal Court of Australia deals with questions of legal professional privilege, following the 8 August 2011 decision of the Federal Court in Hanks v Admiralty Resources NL [2011] FCA 891. In the August 2011 decision, a shareholder in Admiralty Resources NL ('Admiralty') obtained an order under section 247A of the Corporations Act 2001 (Cth) ('the Act') for inspection of the books and records of Admiralty. (The August 2011 decision of the Federal Court was discussed in Item 5.8 of the Corporate Law Bulletin No 169.)

The order of Gordon J made on 8 August 2011 authorised Mr Hanks to inspect the books of Admiralty, relevantly including documents relied on by the directors of Admiralty to assert that an offer to buy shares in its subsidiary was not superior to an earlier offer.

Despite the order, Admiralty refused to produce to Mr Hanks an unredacted minute of a meeting of directors and a memorandum of advice from its solicitors. Mr Hanks therefore applied for an order permitting him to inspect the advice. Justice Gordon dismissed the application for inspection of the advice, holding that an order under section 247A of the Act authorising a member to inspect categories of the books and records of a company does not abrogate legal professional privilege for documents within those categories.

Further, on the facts, Gordon J held that public statements that the board of Admiralty had considered legal advice received in reaching its conclusion did not of themselves disclose the substance of the advice, and were therefore not inconsistent with maintaining the privilege.

Finally, Gordon J in the exercise of her discretion under section 247A refused to order production of the advice on such terms as would maintain the privilege.

(b) Facts

Admiralty Resources NL owned a corporation called Sociedad Contractual Minera Vallenar Iron Company ('VIC'). VIC's main assets were mining tenements in Chile.

On 2 September 2010, Admiralty announced that it had entered into a share sale agreement with Icarus Derivatives Ltd ('Icarus'). The agreement was for the sale by Admiralty to Icarus of shares in VIC.

There was a term of the agreement that Admiralty would not engage in any conduct to solicit, encourage or initiate other offers, or participate in any discussions or negotiations in respect of other offers unless Admiralty's board concluded, on advice, that it had a fiduciary duty to do so.

On 15 September 2010 Admiralty received an offer from Hebei Wenfeng Iron and Steel Co Ltd ('HWF') to purchase VIC. The offer was rejected.

On 28 September 2010, Admiralty gave notice of an extraordinary general meeting to consider the sale to Icarus.

The week before the meeting, Admiralty received a further offer from HWF to purchase VIC. The board of Admiralty met on 27 October 2010, considered legal advice and resolved that the second HWF offer was not superior to the Icarus offer.

At an extraordinary general meeting of Admiralty on 29 October 2010, an executive director of the company said, "the Board has considered the offer and does not believe it is a superior offer. In reaching this conclusion the Board considered legal advice received."

A document presented to shareholders at the annual general meeting of Admiralty on 30 November 2010 and released to the Australian Securities Exchange said, "18/10/10 - Letter from [HWF] dated 18/10/20. Received 21/10/10. 27/10/10 - Board considered letter and legal advice dated 27/10/10 and concluded that offer was not a superior offer".

David Hanks, a member of Admiralty, applied under section 247A of the Act to the Federal Court of Australia for an order that he and his solicitor be authorised to inspect certain categories of the books and records of Admiralty.

Section 247A provides that the court may on the application of a member make an order authorising the applicant or someone on behalf of the applicant to inspect the books of a company or managed investment scheme.

The 8 August 2011 order of Gordon J authorised inspection of documents relied upon by Admiralty's directors to make the statements at the annual general meeting and the extraordinary general meeting that "the Board has considered the offer and does not believe it is a superior offer" and that the offer by HWF was "not a superior offer".

The only two documents in that category were the minutes of a meeting on 27 October 2010 of the board of Admiralty and a memorandum of advice dated 27 October 2010 from Admiralty's solicitors.

(c) Decision

Justice Gordon dismissed the application, holding that privilege had not been waived or abrogated, and declined to permit inspection on such terms as would preserve privilege.

(i) No imputed waiver

The decision was at common law and there is no reference in the judgment to section 122 of the Evidence Act 1995 (Cth), which relates to imputed waiver of privilege. This is presumably because section 131A of the Evidence Act 1995 (Cth), which identifies the "disclosure requirements" to which section 122 applies, is in narrower terms than the equivalent provision in the Evidence Act 1995 (NSW) and the Evidence Act 2008 (Vic).

At common law, whether privilege has been waived depends on whether, viewed objectively and informed by considerations of fairness, there is inconsistency between the conduct of the client and the maintenance of the confidentiality which the privilege is intended to protect (Mann v Carnell (1999) 201 CLR 1).

Justice Gordon observed that in Bennett v Chief Executive Officer of the Australian Customs Service (2004) 140 FCR 101, Tamberlin J had stated that privilege could be waived merely by the disclosure of the conclusion reached in an advice, even if the reasoning is not disclosed.

Her Honour distilled from authorities including Osland v Secretary to the Department of Justice (2008) 234 CLR 275 the propositions that:

whether waiver has occurred is a question of fact and degree;

the critical question is whether the substance or effect of the legal advice has been disclosed; and

whether the disclosure of a conclusion expressed in legal advice without disclosing the reasons amounts to a waiver depends upon a consideration of the context.

On the facts, Gordon J held that the conclusion of the advice and the course of action recommended by the advice were not disclosed.

(ii) No implied abrogation

Privilege is a substantive right conferred by the common law and an important civil right to be safeguarded by the law: Daniels Corporation International Pty Ltd v Australian Competition and Consumer Commission (2002) 213 CLR 543.

Section 247A does not contain clear words expressly abrogating privilege, nor does it contain unmistakable and unambiguous language abrogating privilege by necessary implication. Accordingly, Gordon J held that section 247A cannot be read as authorising the production of document protected by legal professional privilege.

(iii) Discretionary decision refusing to permit limited disclosure while preserving privilege

Section 247B of the Act empowers the court to make orders limiting the use a person who inspects the books may make of information obtained during an inspection permitted under section 247A. This power can be used to permit inspection of privileged material while still maintaining privilege, as in Finn v Firefast Pty Ltd [2004] QSC 203.

However, Gordon J was not satisfied that Mr Hanks needed to inspect the advice in order to decide whether to apply for leave under section 237 of the Act to bring an action on behalf of Admiralty against the directors in relation to the recommendation of the Icarus offer.

Further, her Honour was not satisfied that conditions of inspection giving Admiralty full control over the further dissemination of the advice could be imposed which would protect against the privilege being lost.

Finally, Gordon J was not satisfied that Mr Hanks and Admiralty had a common interest such that privilege would not be lost if inspection of the advice were allowed.

Detailed Contents

4.7 Interpreting rights under unitholders' agreements which intersect with statutory rights

(By Lauren Mickel, Freehills)

AMP Capital Property Nominees Ltd & Anor v Westfield Management Ltd [2011] NSWCA 386, New South Wales Court of Appeal, Giles JA, Campbell JA and Meagher JA, 14 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/nsw/NSWCA/2011/386.html

(a) Summary

This case was an appeal by AMP Capital Property Nominees Ltd ('AMPCN') and UniSuper Ltd ('UniSuper') from a decision of Ward J in favour of Westfield Management Ltd ('Westfield'). The question on appeal was whether AMPCN and UniSuper should be restrained from exercising their voting rights at a meeting of the unitholders called under section 601NB of the Corporations Act 2001 (Cth) ('the Act') to vote in favour of a resolution directing the responsible entity to wind-up a managed investment scheme. In order to resolve the question, the Court of Appeal examined the interaction of the parties' contractual rights under a Joint Venture Agreement ('the JVA') they had entered into and their statutory rights under section 601NB of the Act. The Court of Appeal allowed the appeal.

(b) Facts

The KSC Trust ('the Trust') was a managed investment scheme registered under Part 5C.1 of the Act. The principal asset of the Trust was a shopping centre in Perth. The first appellant, AMPCN, held two-thirds of the units in the Trust as nominee for the second appellant, UniSuper. Westfield held the remaining one-third of the units. AMP Capital Investors Ltd ('AMPCI') was the trustee of the Trust and the responsible entity of the scheme.

Under section 601NB of the Act, members of a registered scheme can vote to wind up the scheme by way of an extraordinary resolution. Section 9 of the Act defines an "extraordinary resolution" in relation to a registered scheme as one "that has been passed by at least 50% of the total votes that may be cast by members entitled to vote".

Given that AMPCN held two-thirds of the shares in the Trust, ordinarily it would have been in a position to carry an extraordinary resolution to wind up the scheme under section 601NB of the Act. However, the terms of the JVA also affected its voting rights. In particular, clause 10.1(a) of the JVA prevented AMPCN from exercising its voting rights to sell the Trust property without the written consent "of the Unitholders". Clause 16.2 of the JVA required that the unitholders exercise their voting rights "so as to most fully and completely give effect to the intent and effect" of the JVA.

Notwithstanding these clauses, AMPCN attempted to wind up the scheme under section 601NB of the Act, which would have resulted in the sale of the shopping centre. Westfield argued that AMPCN's conduct breached its obligations under the JVA, particularly clause 16.2, because directing a winding-up of the scheme would inevitably lead to a sale of the shopping centre without the consent of all of the unitholders. This, in turn, would breach clause 10.1. Westfield sought an injunction to restrain AMPCN, which was granted by Ward J at first instance.

On appeal in the present case, AMPCN and UniSuper argued that clauses 10.1 and 16.2 of the JVA were unenforceable either because section 601NB of the Act was inconsistent with an ability to forgo or fetter a right to vote at a unitholder's meeting or because such a right was also given in the public interest and could not be bargained away. The Court of Appeal upheld the appeal on the grounds that the primary judge erred in interpreting the JVA.

(c) Decision

The main issue for determination was whether AMPCN and UniSuper could be restrained from exercising their voting rights at a meeting of the unitholders called under section 601NB of the Act to vote in favour of a resolution directing the responsible entity to wind-up the scheme in the absence of Westfield's prior written consent.

The specific terms of clause 10.1 of the JVA required that the "written consent of the Unitholders" be given to sell the Trust property and thereafter determine the Trust. The Court held that this phrase meant that the written consent of all of the unit holders was required and not merely the consent of a simple majority, as had been argued by AMPCN and UniSuper. The practical effect of this interpretation was to require Westfield to consent to any sale of the Trust property and winding-up of the scheme.

The Court also held that the primary judge erred in interpreting the words "intent and effect" in clause 10.1(a) as prohibiting a sale of the Trust's property in all circumstances. Delivering the opinion of the court, Meagher JA held that upon the proper construction of clauses 10.1(a) and 16.2 of the JVA, the responsible entity was not prevented from determining the Trust pursuant to the Act and selling the property thereafter.

Although it was not necessary to decide this point in light of its previous conclusions, the Court of Appeal nevertheless concurred with the primary judge that clause 16.2 was not unenforceable in its operation in relation to section 601NB of the Act and would not prevent a member from calling a meeting to consider and vote on a resolution directing the responsible entity to wind up the scheme. Accordingly, both the members and the responsible entity were able to exercise their statutory rights under Part 5C.9 of the Act in relation to winding up the Trust. There was also no provision preventing a unitholder from "contracting out" of its right to exercise the power to vote at such a meeting or from agreeing to vote in a particular way.

(d) Orders

The Appeal was allowed and the orders made by Ward J at first instance were set aside.

Detailed Contents

4.8 A successful application for pooling in a winding up

(By Will Frost, Clayton Utz)

In the matter of Kirby Street (Holding) Pty Limited [2011] NSWSC 1536, Supreme Court of New South Wales, Barrett J, 14 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/nsw/NSWSC/2011/1536.html

(a) Summary

The liquidator of each of forty companies which, while operating, were involved in activities of "bargain" or "discount" retail stores operating under the names "Go-Lo", "Crazy Clark's", "Sam's Warehouse" and "Chickenfeed", applied under section 579E(1) of the Corporations Act 2001 (Cth) ("Act") for an order determining that they constituted a "pooled group".

Section 579E provides that, if the Court is satisfied that it is just and equitable to do so, it may order that a group of two or more companies be pooled for the purposes of a winding up in circumstances where:

"(a) each company in the group is being wound up;

(b) any of the following subparagraphs applies:

(i) each company in the group is a related body corporate of each other company in the group;

(ii) apart from this section, the companies in the group are jointly liable for one or more debts or claims;

(iii) the companies in the group jointly own or operate particular property that is or was used, or for use, in connection with a business, a scheme, or an undertaking, carried on jointly by the companies in the group;

(iv) one or more companies in the group own particular property that is or was used, or for use, by any or all of the companies in the group in connection with a business, a scheme, or an undertaking, carried on jointly by the companies in the group".

A pooling order causes several distinct liquidations, as they affect creditors only, to be administered as if they were a single liquidation, with all available assets applied towards the debts and claims of the creditors of all companies rateably, according to the amounts of their debts and claims and as if they were the creditors of a single company.

Having regard to the interconnectedness of the companies, his Honour ordered that the liquidations be pooled due to "[t]he clear advantages that will flow from bringing these administrations to a conclusion on a consolidated basis".

(b) Facts

Justice Barrett addressed each of the following questions put by Counsel for the liquidator, containing the statutory criteria to be satisfied if a pooling order is to be made:

(i) Is there "a group of 2 or more companies" (section 579E(1))?

His Honour stated that the expression "group" in the opening words of section 579E(1) means no more than a collection or plurality; a "group" exists merely through identification of several companies, without any need to find any connection or shared characteristic. Therefore, the forty companies constituted a "group of two or more companies" for the purposes of section 579E.

(ii) Is each company in the group being wound up (section 579E(1)(a))?

Each of the companies was being wound up and all except company number 40 were subject to the form of creditors' voluntary winding up that follows on from voluntary administration under Part 5.3A of the Act (number 40 was subject to winding up by the Court as a result of a previous order).

(iii) Is at least one of the conditions in sub-paragraphs (i) to (iv) of section 579E(1)(b) satisfied?

For the purposes of this analysis, his Honour determined that at a "functional level", the forty companies were able to be divided into the following four classes:

"Class A" were ultimately responsible for the management of the operations of all forty entities;

"Class B", with one exception, were wholly owned subsidiaries of one company;

"Class C" were the operators of retail stores in Queensland; and

"Class D" operated a retail store in Tasmania.

"Related body corporate" under section 579E(1)(b)(i)?

Having regard to the above, it could not be concluded that each of the forty companies was a "related body corporate" of each of the others. For instance, the structural tests for a related body corporate under section 46(a)(ii) and (iii) of the Act were satisfied as between some, but not all, of the companies.

"Jointly liable for one or more debts or claims" under section 579E(1)(b)(ii)?

Some of the companies were parties to a "deed of cross guarantee" on the basis of which the Australian Securities & Investments Commission ('ASIC') made orders under section 341(1) of the Act granting them relief from certain reporting requirements. However, not all forty companies were party to this deed so that, even if the deed's effect were to make its parties "jointly liable for debts", section 579E(1)(b)(ii) was not satisfied in relation to all forty companies.

"Jointly own or operate property" under section 579E(1)(b)(iii)?

There was no evidence that warranted a finding of joint ownership or operation by all forty companies of any property.

"Business, scheme or undertaking carried on jointly" under section 579E(1)(b)(iv)?

His Honour repeated the test he suggested in Allen v Feather Products Pty Ltd (2008) 72 NSWLR 597 that "if several companies, by arrangement with one another, contributed part of what was required to carry on a single business, the business each element of which came from one or more of them might properly be characterised as a business `carried on jointly' by all of them. `Jointly' does not connote merely action in unison but extends also to circumstances in which there is co-ordinated or co-operative action, with the separate acts of each participant complementing or supplementing acts of the others."

Rather than being a "business" or "undertaking", given the interwoven nature of the group, it was held that a "scheme" had been carried on jointly by them. For instance, a program or plan of action was pursued by all forty companies that was calculated to produce (and did produce) financial results recorded in statements prepared on a consolidated basis.

"Own" property that "is or was used" under section 579E(1)(b)(iv)?

Barrett J rejected an argument that he should not follow the interpretation of this sub-section from Re Australian Hotel Acquisition Ltd [2011] NSWSC 1374, where it was held that property has to be owned at the time of the pooling application. The liquidator argued that it ignored the fact that, in most windings up, the liquidator will usually quickly sell property. For instance, as a result of the sale by receivers and managers of the whole of the business of each company, the companies no longer owned goodwill or items of tangible property of the kind used in the conduct of its business.

However, the liquidator successfully argued that there was one piece of property which satisfied the requirement: the property rights arising out of the deed of cross guarantee that some of the group companies had executed. This created a chose in action. Section 579E(1)(b)(iv) only requires that one company own the relevant property and that one or more group companies "use" it. In this case, group companies "used" the chose in action in connection with the "scheme" carried on jointly by all forty companies.

(iv) What does the evidence show with respect to the matters in section 579E(12) as they may affect the answer to question (v)?

Section 579E(12) of the Act requires the Court to have regard to whether it would be just and equitable to make a pooling order. In this regard, his Honour noted that:

the group of forty companies were, to a significant extent, operated as a single unit rather than as separate entities;

the main trading and operating entities in the group shared common directors and the board of one company was responsible for all material decisions relating to the strategy of the group of forty;

there was significant intermingling of the assets of the companies;

the group had only one bank account with all of the companies creditor invoices being paid from this account;

all of the main trading and operating companies in the group were subject to the deed of cross guarantee pursuant to which they guaranteed the payment of each other's debts; and

the only funds available for distribution to creditors by the liquidator were funds that had been received from the receivers and managers and represented the surplus from the proceeds of sale of the group's assets after payment of secured creditors. Those funds were received as a lump sum and could not be allocated between the respective companies.

(v) Is it just and equitable that the order sought be made (section 579E(1)(b))?

Having regard to the above, it was likely that the creditors of the companies would be advantaged by pooling because of the savings achieved by neither reconstructing the intercompany balances nor unravelling their intermingled finances.

(vi) Does section 579E(10) preclude the making of a pooling order?

In circumstances where it was just and equitable to make the pooling order, his Honour was satisfied that "there is no demonstrated basis for a conclusion that the pooling order sought would materially disadvantage" an eligible unsecured creditor (being the test in section 597E(10)).

(c) Decision

The liquidator sought the following relief:

Order that the property of the ADR Group be combined into a single fund.

Order that the committee of inspection for the pooled ADR Group be initially constituted by [named persons], being those persons referred to in the resolution passed at the meeting of creditors held on 17 December 2010, without the need for a resolution under section 548A of the Corporations Act 2001.

Despite being pooled, the liquidator wished to avoid any residual or associated need to identify the assets of a particular company in the group. For instance, the requirement under section 539 of the Act for a liquidator to lodge six-monthly accounts with ASIC. In addition, the second order sought to ensure that the existing committee of inspection of one company continued as the committee of inspection of the pooled group, without the need for any further resolution of creditors.

Justice Barrett noted that the liquidator required relief under section 579G(1)(d), modifying the Act's application in relation to a winding up. As a result, his Honour ordered the liquidator to submit short minutes containing an order determining that the group be pooled for the purposes of section 579E, together with such additional orders to give effect to the relief sought in relation to the pooled group's reporting requirements and committee of inspection.

Detailed Contents

4.9 Conflict between creditors of insolvent trustee company and unitholders: ''Trustees' indemnity" verses the "clear accounts rule"

(By Lincoln Verass, DLA Piper)

Australian Securities and Investments Commission v Letten (No 17) [2011] FCA 1420, Federal Court of Australia, Gordon J, 12 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/cth/FCA/2011/1420.html

(a) Summary

Receivers and managers of two companies in liquidation, which were each trustees of a trust, sought directions in receivership of two joint ventures. They wished to determine if they were justified in paying to the liquidators the amount of any, and if so, of which, creditors claims contained in proofs of debt lodged with the liquidators of the two companies.

In order for the Receivers to have sufficient money to make payments to creditors, it had to be established that the companies in liquidation were entitled to funds as a result of a 'trustees' indemnity'. Such payment would deplete the trust estate resulting in unit holders recognising a greatly reduced return on their investment. The court agreed with the Receivers' contention that the relevant payments could not be made for two reasons: firstly, that the creditor debts had not been properly incurred by virtue of various breaches of trust, and secondly, that any right to indemnity was extinguished by the 'clear accounts' rule.

(b) Facts

The background facts in this matter were as follows:

Mr Letten was in the business of running unregistered property schemes.

Over a period of years, Mr Letten had established many such schemes involving properties across Australia and New Zealand.

Parties were encouraged to invest in these schemes through various product disclosure statements (PDSs). Each PDS referred to a specific investment opportunity involving units in specific property.

In contrast to the information in these documents, investor monies were intermingled in a single separate account and funnelled by Mr Letten, through the trustee companies of which he was sole director, to the various schemes as funds were required.

The intermingling of these funds was such that tracing was impossible.

Twinview Nominees Pty Ltd ('Twinview') and The Glen Centre Hawthorne Pty Ltd ('TGCH') were trustees of two of such schemes with investors drawn primary from Melbourne.

Unitholders noticed the returns on their investments steadily decreasing. Some investors notified ASIC. Ultimately, ASIC successfully petitioned to have the schemes wound up.

Specific dispute:

Creditors for Twinview and TGCH claim these companies were owed money by virtue of a trustee indemnity for payments made in carrying out their role under the trusts of which they were trustees.

The Receivers claim that no monies should be paid because, firstly, no right to indemnity exists, and secondly, because the trustees were yet to restore certain monies owing to the trust in accordance with the clear accounts rule. The extent of the money argued to be owed was such that, even if a right to indemnity existed at law, the quantum of the money available under that right was reduced to zero.

(c) Decision

(i) Did a right to indemnity exist?

Gordon J discussed authority regarding the trustee indemnity rule. Her Honour noted that, though a trustee is personally responsible for liabilities incurred, they are entitled to be indemnified against those liabilities from trust assets. However, this indemnity only exists to the extent that the trustee has adhered to the terms of their mandate. The mandate will be exceeded where expenses are 'unnecessarily' or 'improperly' incurred. These terms contemplate actions done in bad faith, outside the relevant power, or exercised without the expected standard of care and diligence.

Her Honour noted that even if a position in favour of the plaintiff was taken and the court assumed a right to indemnity existed, no money could be paid out until it was determined whether the trustees had outstanding obligations to restore the trust.

(ii) Were there outstanding monies owed to the trust and if so, did any surplus need to be paid to the trustees?

If a trustee uses trust funds improperly, they must restore those funds to the trust. This 'clear accounts rule' operates such that any right to a trustees' indemnity must be weighed against the liability to restore the trust. This is a quantitative exercise. For example, a trustee owed $50 as a result of a legitimate expense incurred in carrying out their duties under the trust deed, but owing $40 to the trust as a result of improper use of trust funds, only has a right to draw $10 from the trust.

In this matter it was accepted by all parties that the maximum owing to creditors of Twinview was $500,000 and $450,000 in the case of TGCH. Gordon J accepted the Receivers' submission that there were separate breaches of trust that required rectification. These were:

That certain funds should have been secured but were, rather, left exposed to the cash market: Following the purchase of real property under the relevant scheme with funds raised from investors for that purpose, an unanticipated surplus remained. In contravention of the Deed, this surplus was left unsecured and put toward other aspects of the business and was ultimately lost.

Failure to account for certain income and debt: Assets of the trust funds were used as security for debt funding in excess of $3.5 million for a separate, though related, company.

Failure to account for distributions to investors: Under the relevant Deed, proper account needed to be kept of all distributions to investors. Twinview and TGCH paid over large sums of money to a related company. Investors occasionally received distributions from this related company. As the distributions had no relationship to income generated by Twinview and TGCH, this was deemed to be a breach of the requirement to keep proper account of distributions.

Failure to comply with the law: The relevant Deed contained a clause requiring the trustees to comply with the law. At all material times the trustees had been operating an illegally unregistered managed investment scheme. For this reason Gordon J found the Deed to have been breached under this head.

Gordon J accepted expert evidence that the quantum of the amounts to be rectified as a result of the above breaches greatly exceeded the amounts owing under any purported indemnity. As a consequence, the Receivers were directed that they should not pay monies from trust funds to the creditors of Twinview or TGCH.

Detailed Contents

4.10 The consequences of a floating charge that crystallises contemporaneously with a debtor's right of set-off

(By Monali Pandey and Jin Ooi, Corrs Chambers Westgarth)

Bank of Western Australia Limited v National Australia Bank Limited [2011] QSC 379, Supreme Court of Queensland, McMurdo J, 12 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/qld/QSC/2011/379.html

(a) Summary

The Bank of Western Australia Limited (Bankwest) advanced a loan of $10.1 million to Cabarita Pacific Holdings Pty Ltd ('Cabarita') in exchange for a fixed and floating charge over Cabarita's assets. Cabarita and Nojoor Road Developments Pty Ltd ('Nojoor') were joint venturers in a land development. Cabarita approached National Australia Bank ('NAB'), offering up to $3 million of the funds loaned by Bankwest as security in exchange for the ability of Nojoor to draw funds upon NAB immediately and ahead of NAB's approval and documentation of a loan facility to Nojoor. NAB agreed to provide this temporary finance on the condition that Cabarita provide a guarantee and a letter of set-off allowing NAB to apply Cabarita's funds to the loan owed by Nojoor. Nojoor failed to repay NAB's loan when it fell due and NAB issued a demand on Cabarita. By that stage, Cabarita had gone into administration and was in the process of being wound up. It was at this point that NAB learnt of Bankwest's fixed and floating charge over Cabarita's assets. NAB caused Cabarita's term deposits to be closed and the proceeds to be applied to the Nojoor loan. Bankwest brought proceedings against NAB, Cabarita and Nojoor, claiming that Bankwest was entitled to payment of the amounts deposited by Cabarita. The issue was whether NAB's right of set-off was subject to Bankwest's fixed charge over Cabarita's property.

McMurdo J held that NAB was entitled to apply the term deposits to set-off Cabarita's debt to NAB, despite the existence of Bankwest's fixed and floating charge over Cabarita's assets, which was registered with ASIC prior in time. Pursuant to the wording of the Deed of Charge, Bankwest's charge over Cabarita's term deposits became fixed when it entered into the guarantee, which was at the same time as NAB's entitlement to set-off its debt to Cabarita came into existence. In determining the nature of the property over which Bankwest held a fixed charge, McMurdo J held that Bankwest held a fixed charge over Cabarita's term deposits according to the conditions agreed between NAB and Cabarita, i.e. Cabarita's guarantee and NAB's right of set-off. Bankwest's claim was therefore dismissed. NAB only had actual notice of Bankwest's charge after Cabarita had gone into administration. In obiter, McMurdo J stated that the result would have been the same if NAB had had actual notice of Bankwest's assignment before exercising its right of set-off. This was because Bankwest's interests were always limited to the debts as varied by the conditions agreed to between NAB and Cabarita.

(b) Facts

On 29 May 2008, Bankwest and Cabarita entered into a Deed of Charge for Bankwest to lend Cabarita $10.1 million in exchange for Bankwest holding a fixed and floating charge over Cabarita's assets. On 20 June 2008, Bankwest lodged notification of details of the charge and a copy of the Deed of Charge with the Australian Securities and Investments Commission ('ASIC'). Due to the lack of a certificate saying that the charge had been duly stamped, the charge was only provisionally registered until 5 August 2008 when this certificate was provided. Pursuant to section 265(9) of the Corporations Act 2001 (Cth), the charge was taken to have been registered since 20 June 2008. In any case a search of the ASIC register from 20 June 2008 would have revealed the existence of Bankwest's charge.

On 29 July 2008, Bankwest advanced a loan of $10.1 million to Cabarita. Cabarita entered into discussions with NAB to finance a loan in favour of Nojoor for a joint venture to develop land. In exchange for the opportunity for Nojoor to draw upon funds immediately, ahead of NAB's approval and documentation, Cabarita offered to deposit up to $3 million as security for the temporary finance. NAB agreed to this arrangement on the proviso that Cabarita sign a guarantee and a letter of set-off that allowed NAB to apply Cabarita's term deposits in satisfaction of its loan to Nojoor. Cabarita agreed and signed these documents on 1 August 2008. NAB advanced the money without actual knowledge of Bankwest's charge. The uncontested evidence was that on 29 July 2008, NAB requested an external information provider to conduct a search which did not reveal the existence of Bankwest's charge. The search was not conducted directly with ASIC.

On 25 August 2008, NAB offered Nojoor a loan of up to $2.8 million and Cabarita signed a further guarantee and letter of sign-off over these deposits, the terms of which were in materially identical terms to those which it had signed earlier. The loan facility was due to expire on 31 August 2009. Nojoor failed to repay its loan on 31 August 2009. In January 2010, administrators were appointed to Cabarita and its creditors resolved that it be wound up. On 1 March 2010, NAB conducted a search of the ASIC register and became aware of Bankwest's charge for the first time. On 29 April 2010, NAB issued a notice of demand to Cabarita for $2,896,390.66. On 10 May 2010, NAB terminated Cabarita's term deposits and applied the proceeds to the Nojoor loan.

(c) Decision

NAB argued that it was entitled to so apply the term deposits despite Bankwest's charge. Bankwest argued that any relevant entitlement of NAB was subject to Bankwest's fixed charge, such that Bankwest was entitled to payment of the amounts deposited.

(i) Did Bankwest's floating charge become fixed on 1 August 2009 by the signing of the guarantee and/or letter of set-off?

Pursuant to clause 3.3 of the Deed of Charge, a floating charge automatically became fixed if, amongst other things, Cabarita either:

breached clause 9 of the Deed. Clause 9.1 stated that Cabarita was prohibited from creating or allowing another encumbrance in connection with the charged property. 'Encumbrance' was defined to include any 'security interest', which term was defined to include a guarantee; or

dealt with any charged property other than in the ordinary course of business.

McMurdo J was satisfied that Cabarita's 1 August 2009 transaction with NAB was in the ordinary course of Cabarita's business as a land developer and that the floating charge had not become fixed by Cabarita's agreement to a set-off. Her Honour then addressed the other limb of Bankwest's argument, namely whether the charge had become fixed by virtue of Cabarita having breached clause 9 of the Deed of Charge.

It was NAB's submission that since the set-off was in the ordinary course of business, Cabarita had not breached clause 9 of the Deed of Charge as clause 9.3 and clause 9.2 (referring to set-offs that were in the ordinary course of business) operated as exceptions to the prohibition on creating another encumbrance noted in clause 9.1. Her Honour agreed. Bankwest then argued that clause 9 of the Deed of Charge had been breached when Cabarita entered into a guarantee. Her Honour accepted this argument because the exception in clause 9.3 for dealings in the ordinary course of business did not refer to guarantees. With the Deed of Charge having been breached, Bankwest's charge automatically became fixed on 1 August 2009.

(ii) What were the consequences of Bankwest's fixed charge over the term deposits?

The automatic crystallisation of the charge occurred contemporaneously with the signing of the guarantee, making Bankwest the equitable owner of Cabarita's property. Her Honour then asked: what was the nature of the property that Bankwest held an equitable charge over? Was it, relevantly, the property consisting of the term deposits but subject to the terms of the letter of set-off?

Bankwest submitted, amongst other things, that NAB's equitable interest was subject to Bankwest's fixed charge. This notion was premised on the assumption that Bankwest's interest, as a fixed charge, arose prior in time to NAB's entitlement. However, it was by the execution of the first guarantee and letter of set-off that the charge became fixed and it was by that same execution, that NAB's entitlement to set-off came into being. Those two consequences occurred contemporaneously, not sequentially. Further, McMurdo J noted that NAB did not have an equitable interest in Cabarita's property per se.

The guarantee and letter of set-off varied the terms of the contract/s by which NAB's debt to Cabarita (for the term deposits) was payable such that the debts would not have to be paid whilst Cabarita was liable to NAB under its guarantee. Further, NAB could repay its debt to Cabarita by crediting Cabarita's term deposits against a debt owed by Cabarita (as guarantor) to NAB. Her Honour noted that even though the 1 August 2009 agreement between Cabarita and NAB had been made in breach of the Deed of Charge, that did not make it ineffective as a variation of the terms of the debt owed by NAB as NAB had no actual notice of the Bankwest charge or the terms of the Deed of Charge. Her Honour found that the letter of 1 August 2009 was effective in varying the terms of the debt owed by NAB to Cabarita and turned to consider whether equity would intervene by disallowing NAB to raise the same defence against the claim of Cabarita's equitable assignee.

The Court considered the law of set-off and noted that a debt may be set-off against the assignee where the debt comes into existence as a legally enforceable claim before the notice of an assignment, whether or not it is payable before that date. Her Honour found that NAB had exercised its right of set-off without notice of the assignment to Bankwest. In obiter, her Honour noted that even if NAB had had actual notice of the assignment before exercising its right of set-off, the position would have been no different because NAB's actions did not diminish Bankwest's rights as the assignee. Bankwest's rights were always limited to the debts, constituted by the term deposits and according to the conditions agreed between Cabarita and NAB on 1 August 2009. Bankwest's claim was accordingly dismissed.

Detailed Contents

4.11 Application for winding up based on insolvency and just and equitable ground - joint venture broken down

(By Tim Jeffrie, Mallesons Stephen Jaques)

Promoseven Pty Ltd v Bluechip Development Corporation (Cairns) Pty Ltd [2011] QSC 368, Supreme Court of Queensland, Lyons J, 9 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/qld/QSC/2011/368.html

(a) Summary

The case discusses the circumstances where a court will grant an application for winding up of a company in insolvency where there are procedural defects that may taint the application. The case also discusses when the court will use its discretion to order the winding up of a company where it is just and equitable to do so.

The Court held that it would grant leave to order a winding up nunc pro tunc (an order to have an earlier procedural defect remedied), even though the application for leave and the application for winding up were made concurrently. The Court then ordered the winding up of the company on the basis that it was insolvent. In the alternative, the Court noted that it would have also ordered the company to be wound up because it was "just and equitable" to do so.

(b) Facts

Promoseven Pty Ltd ('Promoseven') applied to wind up Bluechip Development Corporation (Cairns) Pty Ltd ('Bluechip'). Bluechip was formed in 2005 as a joint venture between two companies: Promoseven and Prime Project Development (Cairns) Pty Ltd ('Prime') to develop commercial and retail premises and serviced apartments known as the Cairns Central Development. Mr Stephen Burt, a director of Promoseven, was appointed to the board of Bluechip as Promoseven's nominee. Mr Sidney Knell, a director of Prime, was appointed to the board of Bluechip as Prime's nominee. Mr Knell was also the director of several companies in the Prime Group that contracted with Bluechip including managing the Cairns Central Development on behalf of Bluechip and selling the apartments.

HSBC Bank ('HSBC') was the major source of funding for the development, providing $18 million via loans secured by a first ranking mortgage. The development was also funded through shareholder loans extended by Promoseven and Bluechip.

Bluechip had difficulty in selling lots forming part of the Cairns Central Development. By 2010, 15 commercial and residential units had not been sold. At June 2011, Bluechip owed a significant amount of money, including to the Australian Tax Office ('ATO'). While Bluechip had significant assets, those were not seen as readily available. On 7 March 2011, Promoseven filed an application to wind up Bluechip on the grounds of insolvency under section 459P of the Corporations Act 2001 (Cth) ('the Act'), which allows certain categories of people to apply for leave to wind up a company. Promoseven could not apply under the creditor's provisions because it was only a prospective creditor. Promoseven subsequently applied to include an additional justification for winding up, on the grounds that pursuant to section 476(4) of the Act, it was just and equitable to do so given the deteriorating relationship between the joint venture parties. Prime opposed the application.

(c) Decision

The Court granted the application for winding up on the grounds that Bluechip was insolvent. Further, Lyons J held in the alternative that it would be just and equitable to grant the winding up.

In assessing Promoseven's application, his Honour dealt with four specific counter arguments raised by Prime:

that the application was procedurally defective in some way;

that the court should not grant leave for winding up nunc pro tunc;

that Bluechip was not insolvent; and

that it was not just and equitable to grant the winding up.

(i) Procedural defect

Lyons J dismissed the first element of the procedural claim. Prime had argued that his Honour had declined to allow Prime to present an affirmative case to prove Bluechip was solvent, and that this was contrary to Chapter III of the Commonwealth Constitution. Lyons J rejected this argument and held that the exercise of judicial power included the ability to regulate the conduct of litigation, which included the power to make orders to place limitations on the way a party conducts its case. Further, his Honour noted that he had not made an order to confine Prime's case, but that Prime had not taken appropriate actions to affirmatively prove the solvency of Bluechip.

Justice Lyons also dismissed Prime's second element of the procedural claim, that Promoseven had breached section 456A of the Act. Section 465A requires the person applying for an order to wind up a company to advertise the application, and rule 5.6 of the Uniform Civil Procedure Rules 1999 (Qld) ('UCPR') requires that that application must be published at least three days after the application has been made and at least seven days before the date fixed for the hearing. Promoseven had informed another bank of the application to wind up before the three days had expired. His Honour noted that the purpose of the rule was to allow the company to discharge its debts within that three day period, and that the early publication may unduly harm the company. His Honour also noted that the power to dismiss the application on the ground of procedural irregularity. In this case, relying on Wilcox J in Re Dikwa Holdings Pty Ltd v Oakbury Pty Ltd (1992) 36 FCR 274, his Honour rejected the application noting that the early notification by Promoseven caused no prejudice or harm to Bluechip and it was not a case of extensive publication. His Honour also noted that the three day requirement was to allow repayment of debts, and in this case Bluechip was not in a position to pay its debts within that time.

(ii) Granting leave

There were two questions the Court needed to answer in considering whether to grant leave to apply for winding up:

whether to grant leave nunc pro tunc (meaning to make an order correcting a previous error); and

whether the Court should use its discretion to grant leave in the circumstances.

First, according to section 459P(3) of the Act, a contributory must seek leave to apply for an order to wind up a company. Promoseven had not applied for leave before commencing an application to have Bluechip wound up. His Honour rejected Prime's submissions that the Court should deny the wind up application on the basis of the procedural irregularity. Instead, his Honour accepted Promoseven's contention that Rule 5.3 of the UCPR allowed for an application for leave to be heard concurrently with an application to wind up. Relying on case law that establishes that failure to obtain leave was a procedural defect that could be cured, and the Court's discretionary power, his Honour granted leave nunc pro tunc. Accordingly, on the basis that Prime had not initially objected and that Prime had not sought to demonstrate how it had been prejudiced, his Honour rejected this aspect of Prime's argument.

Secondly, Justice Lyons also refused Prime's application requesting that he use his discretion to not grant leave to apply to have Bluechip wound up. Citing the decision of McGarvie J in Fortuna Holdings v Deputy Commissioner of Taxation [1987] VR 83, his Honour noted that there were two branches of the principle outlining where a court could exercise its discretion in rejecting leave to apply for a winding up. The first was where there was no chance of success; and the second was where there was a more appropriate remedy. His Honour rejected Prime's argument that there were appropriate remedies in the Joint Venture Agreement, calling the dispute resolution provisions "long winded" and expressing his lack of confidence that the provisions would resolve the issue.

(iii) Bluechip's insolvency

His Honour applied a "cash flow" test in assessing whether Bluechip was insolvent. Bluechip had debts totalling over $1 million that were due and payable. In considering Bluechip's assets, his Honour had regard to physical assets but did not give any weight to the prospect that Bluechip would gain cash from the sale of the Cairns Central Development units in the near future. In addition, his Honour noted that HSBC had refused to provide further finance. On these bases, his Honour concluded that Bluechip was insolvent.

(iv) Just and equitable grounds

Promoseven made an additional application seeking winding up under section 467(4) of the Act on just and equitable grounds. Relying on jurisprudence regarding relief given where partnerships and joint ventures break down, his Honour set out a number of facts that suggested the joint venture had fallen apart or where there had been irregularities. This included a substantial difference in the maturity date between loan agreements and that Mr Knell had admitted to a third party that he had not advised Mr Burt of the difference. His Honour further noted the difficulties in selling units to companies owned by Mr Knell and certain irregularities regarding payments between Bluechip and companies within the Prime Group. Finally, his Honour considered the nature of the relationship between Mr Burt and Mr Knell, noting that it had gradually deteriorated and that there was a significant level of hostility between the parties. His Honour did not accept that there remained any prospect of reconciliation.

Accordingly, his Honour held that in the alternative he would have ordered Bluechip to be wound up on just and equitable grounds.

Detailed Contents

4.12 Icelandic proceeding concerning the winding up of Landsbanki a foreign main proceeding for the purposes of the Model Law on Cross-Border Insolvency

(By Dylan Barber, Blake Dawson)

Backman v Landsbanki Islands hf [2011] FCA 1430, Federal Court of Australia, Jacobson J, 7 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/cth/FCA/2011/1430.html

(a) Summary

Landsbanki, an Icelandic bank, fell into financial difficulties during the global financial crisis. The Icelandic Financial Supervisory Authority appointed a Resolution Committee which successfully applied to have Landsbanki wound up. The plaintiffs, who were appointed as members of the Winding-up Board, applied to the Federal Court of Australia to have the winding-up proceeding in Iceland recognised as a "foreign main proceeding" for the purposes of the Model Law on Cross-Border Insolvency, which has the force of law in Australia. Jacobson J determined that the Icelandic proceeding was a foreign main proceeding for the purposes of the Model Law. The matter was stood over until March 2012 in order for the plaintiffs to seek such relief that may be available to a registered liquidator given the circumstances that present when the matter is next before the court.

(b) Facts

Landsbanki Islands hf ("Landsbanki") was a full service bank which provided retail, corporate and investment banking services. Landsbanki was incorporated in Iceland and had its registered office in Reykjavik.

In October 2008, during the global financial crisis, the Icelandic Parliament passed legislation to permit the Financial Supervisory Authority of Iceland to take measures to minimise instability and harm to financial markets as well as to allow for the reorganisation and winding up of banks and other financial institutions.

Landsbanki subsequently fell into financial difficulties and the Financial Supervisory Authority appointed a Resolution Committee to assume control of the bank (it was submitted that the role of the Resolution Committee was similar to the role of a voluntary administrator under the Corporations Act 2001 (Cth)).

The Resolution Committee successfully applied to the District Court in Reykjavik to have Landsbanki wound up. The Resolution Committee appointed a Winding-up Board in order to administer aspects of the reorganisation and winding up that did not fall within the ambit of the authority held by the Resolution Committee. The plaintiffs were appointed members of the Winding-up Board by the District Court on 29 April 2009.

The plaintiffs brought the current proceeding on behalf of the Winding-up Board to determine whether the Icelandic proceeding concerning the administration and winding up of Landsbanki was a "foreign main proceeding" for the purposes of the Model Law on Cross-Border Insolvency ('Model Law'). Section 6 of the Cross-Border Insolvency Act 2008 (Cth) provides that the Model Law has the force of law in Australia.

Article 20 of the Model Law provides that upon recognition as a foreign main proceeding:

commencement or continuation of actions or proceedings in relation to the debtor are stayed;

execution against the debtor's assets is stayed; and

any right to encumber or dispose of any assets of the debtor is suspended.

Article 21 of the Model law provides that a court is permitted to grant relief in terms which reflect the provisions in Article 20, as well as any other appropriate relief including "any additional relief that may be available to a registered liquidator".

(c) Decision

Article 17 of the Model Law contains the criteria for determining whether a proceeding shall be recognised as a foreign main proceeding.

Jacobson J considered it important to note that the Icelandic proceeding had previously been recognised as a foreign main proceeding by courts in both the United States of America and Canada.

(i) Decision to recognise as a foreign proceeding

Jacobson J was satisfied that the first two requirements of Article 17 of the Model Law, that the Icelandic proceeding was a collective judicial or administrative proceeding in a foreign state for the purpose of reorganisation or liquidation and that the applicant for recognition was a person or body authorised in a foreign proceeding to administer the reorganisation or the liquidation, had been met. The plaintiffs had been appointed by the District Court in Reykjavik, were subject to supervision by the District Court and held the relevant powers.

The plaintiffs provided certain certificates, including a certified copy of the decision commencing the foreign proceeding and a certificate from the foreign court affirming the existence of the foreign proceeding, in order to satisfy the third requirement.

In addition, the Federal Court of Australia, in which the current proceeding was being heard, was a relevant court for the purposes of the Model Law, resulting in Jacobson J being satisfied that all of the requirements for the recognition of a foreign proceeding pursuant to the Model Law had been met.

(ii) Decision to recognise as a foreign main proceeding

Pursuant to the Model Law, in order for the foreign proceeding to be recognised as a foreign main proceeding the foreign proceeding must be taking place in the State where the debtor has the centre of its main interests.

Jacobson J considered that the evidence of the plaintiffs established that Iceland was the centre of Landsbanki's main interests. In any event, the Model Law presumes that the location of Landsbanki's main office (which was in Iceland) was also the centre of Landsbanki's main interests.

(iii) Decision upon recognition as a foreign main proceeding

As such, Jacobson J was satisfied that the Icelandic proceeding was a foreign main proceeding for the purposes of the Model Law. However, the terms of the order sought by the plaintiffs, that the plaintiffs be afforded all powers available to liquidators appointed under the Corporations Act 2001 (Cth), were too broad.

Instead Jacobson J stood the matter over until March 2012 in order for the plaintiffs to seek such relief that may be available to a registered liquidator given the circumstances that present between the date of this hearing and when the matter is next before the court.

Detailed Contents

4.13 ANZ class action: bank fees can be penalties only if payable on breach

(By Jack Hill, Solicitor, Mallesons Stephen Jaques)

Andrews v Australian and New Zealand Banking Group Limited [2011] FCA 1376, Federal Court of Australia, Gordon J, 5 December 2011

The full text of this judgment is available at:

http://www.austlii.edu.au/au/cases/cth/FCA/2011/1376.html

(a) Summary

This decision clarifies the law regarding penalties and rejects attempts to increase the reach of the principle beyond the realm of contractual breach. It affirms that breach of contract is a necessary element for the law of penalties to apply, and that the law of penalties is a narrow exception to the general rule that the law seeks to preserve freedom of contract, allowing parties the widest freedom to agree upon the terms of their contract.

(b) Facts

The case involves a large representative action brought by ANZ customers regarding the validity and enforceability of a wide variety of fees imposed by ANZ under the terms of certain banking products.

This decision dealt with the preliminary question of whether the fees were capable of being characterised as penalties.

The fees in question included:

honour fees - fees imposed where a debit that is honoured by ANZ, at its discretion, causes an account to go into overdraft;

dishonour fees - fees imposed where a debit which would cause an account to go into overdraft is dishonoured by ANZ, at its discretion;

overlimit fees - fees incurred when ANZ allows a credit card account to exceed a pre-agreed limit;

non-payment fees - fees incurred when a periodic payment cannot be made on an account because there are insufficient cleared funds; and

late payment fees - fees incurred when a payment due is not paid by the required date.

The fees outlined above were collectively referred to by the court as "exception fees". The applicants sought declarations that the exception fees were void or unenforceable as penalties.

The applicants argued that the exception fees were incurred as a consequence of a breach of the relevant arrangement with ANZ and therefore were capable of constituting penalties. Alternatively, the applicants argued that breach of contract is not an essential element of the law of penalties, and that the exception fees could constitute penalties as they formed part of a contractual mechanism designed to protect the interests of ANZ by discouraging certain conduct by customers.

(c) Decision

The court found that only the late payment fees were incurred as a direct result of a breach, namely a failure to pay within the required time. Consequently, the court held that the late payment fees were capable of constituting penalties.

The court rejected ANZ's characterisation of the late payment fee as an additional fee charged in connection with the operation of the account reflecting, in part, the increased risk associated with the account when repayments were not made within the specified time. The court found that the fee was properly characterised as a payment consequent upon breach, and that it was for ANZ to seek to justify the size of the fee during the next stage of the proceedings. ANZ conceded that the exception fees were not a genuine pre-estimate of its damages.

Following a detailed analysis of the history of the law of penalties, Gordon J found that "there is extensive and long standing authority in Australia and the United Kingdom that the law of penalties has no application to a contractual provision requiring payment on the happening of an event that does not constitute a breach of contract."

In distinguishing the late payment fees from the other exception fees, the court found that the late payment fees were imposed as a result of a unilateral action by the applicant which was a breach of their contract with ANZ (being a failure to pay an amount by the due date). However, the other exception fees were imposed as a result of a discretionary action by ANZ in response to a request from an applicant (for example, to overdraw the applicant's account). This action was not unilateral and required the consensual conduct of ANZ and the applicant and therefore could not constitute a breach by an account holder. Accordingly, Gordon J found that the other exception fees were not capable of being characterised as penalties.

(i) The law of penalties is confined to payments for breach of contract

In reaching the conclusion that only the fees chargeable as a direct result of an account holder's breach were capable of being characterised as penalties, Gordon J relied upon a long list of Australian and UK authorities. In particular, her Honour had regard to the decision of Ringrow Pty Ltd v BP Australia Pty Ltd (2005) 224 CLR 656. In Ringrow, the High Court unanimously stated that "the law of penalties, in its standard application, is attracted where a contract stipulates that on breach the contract-breaker will pay an agreed sum which exceeds what can be regarded as a genuine pre-estimate of the damage likely to be caused by the breach."

Gordon J rejected the applicants' argument that the reference to "standard application" amounted to an acknowledgment by the High Court that there was, and remains, some other class of penalty which could be struck down and that this other class was one in which breach was not a necessary element. Her Honour noted that by using the phrase "standard application" the High Court was merely identifying that the law of penalties addressed two different cases; cases where money is payable and cases where money's worth (including property) is transferable on the happening of an event that constitutes a breach of contract.

Her Honour acknowledged that judicial statements indicating that breach is not an essential element of the law of penalties are rare.

Her Honour also considered a recent decision of Brereton J in Integral Home Loans Pty Ltd v Interstar Wholesale Finance Pty Ltd [2007] NSWSC 406 (which was overturned by the New South Wales Court of Appeal), upon which the applicants placed significant emphasis. In that decision, Brereton J held that the law of penalties was not limited in its application to circumstances where a contract is terminated for breach but that its scope extended to circumstances where a contract is terminated pursuant to a right to do so upon occurrence of an event of default which the non-terminating party had, in substance, an obligation to avoid. Gordon J rejected this analysis, noting that the extended rule finds support neither in Australian authority, decisions in other common law jurisdictions, nor in the history of the law.

(ii) Matters to be determined at the next stage of the proceeding

At the next stage of the proceedings, ANZ will be required to justify the size of the late payment fees having regard to the burden they impose on customers compared with the loss incurred by ANZ due to the breach. If the court decides that these fees are in fact penalties, they will be ruled void.

Detailed Contents

5. Contributions

If you would like to contribute an article or news item to the Bulletin, please email it to: "cclsr@law.unimelb.edu.au".

Detailed Contents

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Sent to : i.ramsay@unimelb.edu.au