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1. RECENT CORPORATE LAW AND CORPORATE GOVERNANCE DEVELOPMENTS

(A) APRA PROPOSES BLUEPRINT FOR FUTURE REGULATION OF GENERAL INSURANCE

On 26 September 2002 The Australian Prudential Regulation Authority (APRA) provided its Submission to the HIH Royal Commission on Future Policy Directions for prudential regulation of the general insurance industry.

This is APRA's response to a request by the Commission to provide its views on improvements in the regulation of insurance. While the recommendations centre upon the general insurance industry, many of the initiatives can be appropriately applied across the financial services industry in line with the integrated regulatory model adopted by APRA.

The three main areas where APRA proposes further improvements are:

(1) Consolidated supervision - it is essential that prudential supervision be applied across the whole of insurance groups on a consolidated basis, including their international operations, as well as focusing on the individual Australian insurers that are members of these groups.

(2) Disclosure - APRA is committed to improving the quality of insurance companies' disclosure to the market about their risk-adjusted financial strength and performance relevant to their ability to pay policy claims.

(3) Corporate governance and risk management - the Submission identifies areas for potential governance reform which aim to keep Boards and others honest, open, diligent and accountable by upgrading their responsibilities. Such measures could include:

- Personal attestations by directors and senior executives - requiring annual sign-off by individual directors and senior executives of regulatory compliance;
- Peer review of actuarial reports - the development of a process by which actuarial reports are subject to independent review to ensure appropriate standards are maintained;
- Separation of audit and actuarial firms - consideration will be given to prohibiting the use of actuaries and auditors from the same firm;
- Financial condition reports - a requirement for an Approved Actuary to carry out an overview of a company's financial soundness, not just its insurance liabilities;
- Whistle-blowing protection - protection for company directors and officers that advise APRA of issues they consider have the potential to damage policyholders' interests.

In addition, APRA recommends amendments to legislation to increase its enforcement powers; its operational independence; and its ability to deal with insurance-type activities that do not presently come under the [Insurance Act 1973 No. 76 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=6398" \t "default).

In its Submission, APRA also canvasses options for a compensation scheme that would be activated in the event that a general insurer, or other regulated entity, fails.

A copy of APRA's Submission is available at [http://www.apra.gov.au/](http://www.apra.gov.au/%22%20%5Ct%20%22_new).

(B) REVIEW OF INDEPENDENT COMPANY AUDITING

In a media release dated 18 September 2002 Mr Bob Charles MP, Chairman of the Joint Committee of Public Accounts and Audit, announced that the Australian Federal Parliament's Public Accounts and Audit Committee had made 13 recommendations for changes to Australia's corporations law, corporate governance standards and private sector auditing practices following a six-month investigation of these issues.

Conducted in the wake of corporate collapses in Australia and overseas, the 144-page review of independent auditing by registered company auditors was released in parliament on 18 September 2002.

Key recommendations include:

- Amending the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) to clarify and enforce the requirement that directors and auditors must certify that accounts both comply with Australian accounting standards and represent a true and fair view of the company's affairs;
- Requiring CEOs and Chief Financial Officers of companies to sign statutory declarations attesting that the company's financial reports comply with the Corporations Act and are materially truthful and complete;
- Requiring all publicly listed companies to have an independent audit committee, with the Corporations Act prescribing minimum requirements which the committee must meet;
- Amending the Corporations Act to require audit firms to detail annually to the Australian Securities and Investments Commission (ASIC) how they are dealing with independence issues, reporting against benchmarks set by ASIC;
- Amending the Corporations Act to require auditors to report on whether the auditor believes a company is complying with new corporate governance standards to be developed by the Financial Reporting Council (including prescriptions for internal audit);
- Amending Australian Stock Exchange (ASX) Listing Rules to require additional reporting by companies against a range of criteria and performance indicators; and
- Introducing greater protection for auditors by replacing the principle of joint and several liability with proportional liability; allowing auditors to work within limited liability structures; and introducing a cap for professional liability claims, to limit damages awarded against auditors.

The full report is available on the Joint Committee of Public Accounts and Audit website at [http://www.aph.gov.au/house/committee/jpaa/indepaudit/contents.htm](http://www.aph.gov.au/house/committee/jpaa/indepaudit/contents.htm%22%20%5Ct%20%22_new)

For information and background on the inquiry, contact the inquiry secretary, Mr Adam Cunningham on (02) 6277 2336, or visit the inquiry website at [http://www.aph.gov.au/house/committee/jpaa/Indepaudit/inqinde2.htm](http://www.aph.gov.au/house/committee/jpaa/Indepaudit/inqinde2.htm%22%20%5Ct%20%22_new)

(C) GOVERNMENT ANNOUNCES POLICY PROPOSALS ON AUDIT REGULATION AND CORPORATE DISCLOSURE

On 18 September 2002 the Australian Federal Government released a comprehensive set of policy proposals on audit regulation and the wider corporate disclosure framework. The paper, "Corporate Disclosure: Strengthening the Financial Reporting Framework", is the next chapter in the Government's Corporate Law Economic Program and will be known as CLERP 9.

The paper proposes a fundamental reshaping of the financial reporting framework. It builds on existing institutions and clarifies responsibilities to focus on the quality of financial reporting.

Under the proposals the Government will, among other things:

- Expand the role of the Financial Reporting Council to include public oversight of audit independence and audit standard setting in Australia. Auditing standards will also have the force of law on the same basis as accounting standards issued by the Australian Accounting Standards Board.
- Make audit committees mandatory for Australia's top 500 listed companies.
- Make audit partner rotation compulsory after 5 years.
- Amend the law to require disclosure in annual reports of fees for all categories of all non-audit services provided by an audit firm.
- Amend the law to require audit committees to certify that receipt of certain non-audit services did not compromise audit independence.
- Amend the law to increase the maximum civil penalty for contraventions of continuous disclosure provisions from $200,000 to $1 million.
- Amend the law to give the Australian Securities and Investments Commission the power to impose financial penalties and issue infringement notices in relation to contraventions of the continuous disclosure regime.
- Amend the law to provide penalties for retaliation against a company employee who reports to ASIC a suspected breach of the law in good faith and on reasonable grounds.
- Reform areas of auditor liability by allowing auditors to incorporate and seek agreement of the States to introduce proportionate liability.
- Revise civil and criminal penalties applying to financial reporting offences to ensure consistency and adequacy.
- Establish a Shareholders and Investors Advisory Council to provide advice on disclosure reforms to ensure they meet the needs of retail investors.
- Encourage shorter, more comprehensible notices of meetings and facilitate improved shareholder participation by electronic means.

The paper incorporates the Government's response to the report of Professor Ramsay on auditor independence. The Government has adopted virtually all of Professor Ramsay's recommendations.

The Government will continue to consult with business and the community on these proposals. Consultation will close on 22 November 2002. The Government will then release exposure draft legislation for comment, with legislation expected to be introduced early in 2003.

Copies of the paper are available from the Treasury website at [http://www.treasury.gov.au/](http://www.treasury.gov.au/%22%20%5Ct%20%22_new)

\* Comments on the paper should be sent to:

General Manager
Corporate Governance Division
Department of the Treasury
Langton Crescent
Parkes ACT 2600

Submissions are due by 22 November 2002. As submissions may be made public, any confidential material should be marked accordingly.

(D) APRA CRITICISES AUDIT PERFORMANCE

On 17 September 2002 the Australian Prudential Regulation Authority's (APRA) General Manager, Dr Darryl Roberts, told an Association for Compliance Professionals of Australia Incorporated (ACPA) seminar on "Compliance versus Enforcement" that the practice of auditor certification was working well below par.

Speaking at the ACPA/PricewaterhouseCoopers conference in Sydney, Dr Roberts said "While a key element of APRA's prudential safety net, our experience is that in many cases we cannot take much comfort from the work of the external auditor."

"A disturbing number of auditors seem ignorant of the relevant statutes and standards, and are failing to detect and flag weaknesses such as non-compliance with APRA prudential standards," Dr Roberts told conference delegates.

Cited among the areas of concern within regulated financial institutions, that auditors were failing to identify, were:

- delegations set at inappropriate levels of seniority;
- large credit exposures that breach prudential limits;
- lack of a strong, independent internal audit function;
- inadequate controls on lending to related parties; and
- inadequate controls on risky activity.

"The compliance function should be deeply embedded in a financial institution's everyday commercial culture, and not regarded as a mere mechanical or legalistic box-ticking exercise," said Dr Roberts.

For the financial year ended 30 June 2002, APRA will be questioning auditors where its on-site activity identifies compliance problems but the audit report remains unqualified.

Dr Roberts also highlighted the accountability of the board and senior management of regulated institutions.

"If APRA detects a failure to exercise good risk management - for example, serious problems are swept under the carpet - then we will not hesitate to deem board members and senior executives unfit for their roles and remove them," he said.

A copy of Dr Robert's presentation is available on APRA's website at [http://www.apra.gov.au/](http://www.apra.gov.au/%22%20%5Ct%20%22_new).

(E) U.S. COMMISSION CALLS FOR MAJOR EXECUTIVE COMPENSATION REFORMS

On 17 September 2002 the United States Conference Board's Blue-Ribbon Commission on Public Trust and Private Enterprise proposed a wide-ranging series of reforms to strengthen corporate compensation practices.

The twelve person Blue Ribbon Conference Board Commission on Public Trust and Private Enterprise is comprised of major business leaders, major investors, former senior government and regulatory officials as well as a university professor of business ethics.

This report, the first in a series of three reports, focuses on executive compensation. Subsequent reports will deal with reforms on other areas of corporate governance as well as accounting and auditing issues.

The Conference Board Commission on Public Trust and Private Enterprise said, "it shares the public anger at the misconduct leading to the breakdown in public trust." Commission Co-Chair Peter G Peterson, Chairman of The Blackstone Group, noted the "lack of fairness" of the unprecedented levels of executive compensation, particularly the compensation of certain executives, even as their companies and the retirement savings of their employees have collapsed. Co-Chair John W Snow, Chairman, CSX Corporation, added, in referring to the malfeasance at Enron, WorldCom and other companies: "these egregious failures evidence a clear breach of the basic contract that underlies corporate capitalism." The Commission proposed wide ranging reforms on executive compensation including:

- retention and direction of compensation experts by compensation committees - not management;
- compensation committees setting compensation not by ratcheting up industry averages;
- uniformly expensing stock options;
- substantial director and top management stock ownership for extended holding periods;
- avoiding "special purpose entity" compensation to executives;
- greater disclosure of equity dilution and employment agreements;
- shareholder approval of option repricing; and
- advanced notice of executive stock sales.

(1) 'Excessive use' of stock options

The report declares that: "Executive compensation has become too 'delinked' from long-term performance goals in many corporations. There is an imbalance between unprecedented levels of executive compensation, with little apparent financial downside risk or relationship of this compensation to long-term company performance."

(2) Four guiding compensation principles

The Committee suggests a series of recommended principles as well as a series of specific best practices. The principles include:

(a) Focus on a much tighter linkage between executive operating performance and executive compensation, rather than simply on the ups and downs of the stock market, which are often not closely related to the executive's contribution to the long-term value of the enterprise.

(b) Focus on a fully independent, accountable, and vigorous compensation committee that takes primary responsibility for all aspects of executive compensation including employment, retention, and severance agreements.

(c) Focus on accounting neutrality so as to avoid bias and favour of any one form of equity based compensation, and, at the same time, facilitate comparability of results as between companies.

(d) Focus on full disclosure of all material information on an understandable and timely basis and, in particular, to reassure the public that management is not involved in stock transactions with advanced knowledge of material information not available to the public at that time.

(3) Recommended best practices

(a) The Compensation Committee should retain any outside consultants who advise it, and the outside consultants should report solely to the Committee.

(b) The Compensation Committee should be unconstrained by industry averages and statistics or by the company's past compensation practices and levels, which, in certain companies, have been excessive.

(c) Stock options should be expensed on a uniform and broadly accepted basis. This will eliminate the accounting treatment that makes stock options so desirable to companies at the expense of more performance-oriented forms of compensation including cash, and equity compensation.

(d) Senior management and directors should: 1) be required to own a meaningful amount of company stock on a long-term basis; and 2) be subject to substantial minimum holding periods for equity received as compensation, in each case in order to align the interests of management with those of the corporation. Holding periods for senior executives and directors should generally not be less than the holding periods for other employees.

(e) Companies should avoid the use of special purpose entities to compensate or enrich senior executives.

(f) There should be a strengthening of requirements for conspicuous disclosure of all material impacts of stock options and other compensation arrangements, including overall costs and earnings dilution effects, as well as disclosure of all employment agreements for top executives, including severance arrangements.

(g) Shareholders should approve modification of existing equity compensation arrangements, including repricing options or any actions that could dilute their holdings.

(h) Executive officers should be required to give advanced public notice of their intention to sell their stock.

(4) Commission will launch new national effort

The Commission applauded the new [Sarbanes-Oxley Act](http://www.loc.gov/law/guide/pl107204.pdf%22%20%5Ct%20%22_new) and new stock exchange rules as actions to curb further abuses. The Commission will launch a national effort to encourage corporations and investors to take their own corrective actions by installing a series of recommended best practices and thus avoid additional legislation on executive compensation. As an example of the unintended effects of such legislation, the Commission pointed to earlier tax legislation and the intention to limit executive pay by disallowing tax deductions in excess of $1 million. Instead of accomplishing its intended purpose, this legislation contributed to fixed-price options becoming the dominant form of executive compensation.

The report is available on the Conference Board's website at [http://www.conference-board.org/](http://www.conference-board.org/%22%20%5Ct%20%22_new).

Members of The Conference Board's Commission on Public Trust and Private Enterprise include:

Peter G Peterson, Chairman of The Blackstone Group, former Secretary of Commerce and Chairman of the Federal Reserve Bank of New York
John W Snow, Chairman, CSX Corporation and former Chairman, Business Roundtable
John H Biggs, Chairman, President and CEO, TIAA-CREF
John C Bogle, Founder and former Chairman, Vanguard Group, Inc
Charles A Bowsher, former Comptroller General
Peter M Gilbert, Chief Investment Officer, State Employees' Retirement System, Commonwealth of Pennsylvania
Andrew S Grove, Chairman of Intel Corporation
Ralph S Larsen, former Chairman and CEO of Johnson & Johnson, former Chairman of The Business Council
Arthur Levitt Jr, former SEC Chairman and former Chairman of the American Business Conference
Professor Lynn Sharp Paine, John G McLean Professor of Business Administration Harvard Business School
Former Senator Warren B Rudman, Paul, Weiss, Rifkind, Wharton & Garrison
Paul A Volcker, former Chairman of the Board of Governors, Federal Reserve System

(F) SUPERANNUATION REGULATIONS DISALLOWED IN THE SENATE

On 16 September 2002 the Australian Labor Party combined with minor parties in the Senate to disallow the superannuation product disclosure regulations which had been made under the [Financial Services Reform Act 2001 No. 122 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=58127" \t "default). The regulations which have been disallowed put in place a heightened disclosure regime for superannuation products, including disclosure of the ongoing management charge for superannuation products. The reasons put forward by the Labor Party for disallowing these regulations included criticisms of the ongoing management charge and also criticism of the fact that the enhanced disclosure applied only to superannuation products and not to other types of managed investments.

The result is that Schedule 10B of the [Corporations Regulations 2001 No. 193 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56758" \t "default) is no longer effective and the special disclosure rules contained in that Schedule for superannunation products no longer apply. This means that the disclosure requirements applying to superannuation products are regulated solely by Part 7.9 of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default).

It has been suggested that product disclosure statements that have been prepared on the basis of complying with Schedule 10B can still be used provided they meet the requirements of Part 7.9 of the Corporations Act.

(G) SURVEY FINDS IMPROVED CORPORATE GOVERNANCE

The events of the last year have had a positive impact on the governance practices of corporate Australia a new survey has found, with an overwhelming number of companies overhauling their audit, disclosure and risk management practices.

According to the Chartered Secretaries Australia (CSA) survey of company secretaries in the Australian Stock Exchange Top 200 companies (published on 12 September 2002), 83 per cent have reviewed and improved their processes and procedures. Not surprisingly, a review of audit practices topped the list of 'must dos'. Also, many companies reported an increase in focus at Board and CEO levels on the importance of corporate governance.

Organisations have opted for wide-ranging improvements including the revision of the Audit Committee Charter, full disclosure of the relationship with auditors, and mandating that the auditors cannot provide other services. In addition 86 per cent of respondents are satisfied with the progress being made towards ensuring auditor independence in Australia.

The survey also found an increased focus on annual reporting particularly in terms of share options and audit committee function reporting.

The vast majority - 89 per cent - of company secretaries believe investors will increasingly reward companies with sound, transparent corporate governance practices and punish those with questionable ones.

There is also strong support for the United States' requirement for CFOs and CEOs to verify the accuracy of the accounts with 79 per cent of respondents agreeing that it will help restore investor confidence.

Increased accountability and deterrents are perceived as a key part of improving investor confidence, yet relatively few criminal convictions for corporate crimes are successful. In this context, 73 per cent of respondents believe the option of a civil action for such crimes would increase the chance of conviction, help recover losses for the company and act as a stronger deterrent.

There was little support for corporate governance practices in Australia to be regulated by the listing rules and enforced by the ASX (34 per cent) or by legislation enforced by the ASIC (30 per cent).

61 per cent of respondents believed there should be no change in the way corporate governance is currently regulated.

(H) DIRECTORS' PERSONAL LIABILITY UNDER EXAMINATION

On 11 September 2002 the Hon Senator Ian Campbell, Parliamentary Secretary to the Treasurer issued a press release advising that the Australian Federal Government had asked the Corporations and Markets Advisory Committee to identify any inconsistencies and compliance cost overlaps in existing laws relating to directors' liability.

Senator Ian Campbell said the committee would investigate the personal liability of directors at common law and under Federal and State/Territory statutes.

"The business judgement rule which came into effect two years ago as a result of the CLERP 3 reforms addressed directors' duty of care and diligence, however directors are also subject to a range of other duties and requirements by the Commonwealth, States and Territories," Senator Campbell said.

"Concerns have been raised that overlapping and inconsistent duties and potential liabilities are generating unnecessary compliance burdens and causing difficulties in obtaining insurance cover.

"The purpose of this examination is to identify the full range of impacts of existing laws with a view to rationalising the various requirements and duties."

He said the committee would also consider whether potential personal liability under the various requirements were disincentives to anyone considering board positions.

The committee is expected to start its investigation soon.

(I) FEDERAL GOVERNMENT RELEASES FINANCIAL SERVICES COMPENSATION ISSUES PAPER

On 6 September 2002 a Federal Government paper on compensation for loss in the financial services sector was released for public discussion.

The paper discusses issues and options for compensation for loss suffered by clients for any financial product. It includes services for market-traded products, those traded outside formal markets and those for which there is no secondary market.

It also includes financial products which are in the nature of investments as well as products designed to manage risk. It does not, however, cover loss caused by market fluctuations or the failure of the institution that issued the product.

The paper is available on the Treasury website at [http://www.treasury.gov.au/](http://www.treasury.gov.au/%22%20%5Ct%20%22_new) and in Commonwealth Government bookshops. There will be a two-month public exposure period.

(J) INSIDER TRADING PROPOSALS PAPER

On 3 September 2002 the Corporations and Markets Advisory Committee published a paper on insider trading proposals. Following is an extract from the paper's Introduction.

(1) The current review

- The Advisory Committee is currently reviewing Australia's insider trading laws.
- In undertaking this review, the Advisory Committee saw the need for clear and effective laws to protect and guide Australian financial markets. Lack of clarity can result in reduced compliance as well as unproductive uncertainty for market participants. Where necessary, insider trading laws should be strengthened to make them fully effective and assist enforcement. These laws should also not impede legitimate market activity.

(2) Earlier Discussion Paper

- The Advisory Committee published its Insider Trading Discussion Paper in June 2001. That Paper set out a framework for general debate, as well as raising specific issues, on the appropriateness of the insider trading laws for Australian financial markets. That Paper also contained a detailed legal analysis of insider trading laws in Australia and overseas jurisdictions. The Discussion Paper is available on the CAMAC website at [http://www.camac.gov.au/](http://www.camac.gov.au/%22%20%5Ct%20%22_new).

(3) Legislative developments

- The application ambit of the insider trading laws has been considerably extended since the Discussion Paper was published in June 2001. In March 2002, the [Financial Services Reform Act 2001 No. 122 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=58127" \t "default) (FSRA) introduced amendments into the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) to harmonise the regulation of financial markets and services. These amendments included extending the insider trading laws beyond securities (including a limited class of over-the-counter-traded securities) and some futures contracts to a very broad range of financial products, including all derivatives, as well as any other financial products that can be traded on a financial market.

(4) Proposals Paper

- This Proposals Paper discusses the implications of the above developments, as well as the Advisory Committee's current thinking on the other matters raised in the Discussion Paper. Before settling its Final Report, the Advisory Committee takes the opportunity to outline, and seek comments on, important issues that have arisen in the review. The Paper is structured as follows.

(a) Chapter 1

- This Chapter outlines the key characteristics of the various financial markets that operate in Australia and the implications of the current insider trading laws for each of these markets. It raises for consideration various options on how best to apply the insider trading laws to each of those markets.

(b) Chapter 2

- This Chapter discusses the merits of introducing various statutory exemptions, independently of the matters discussed in Chapter 1, in areas where the application of the insider trading laws may be inappropriate. Areas discussed include share issues, buy-backs, off-market transactions in exchange-tradeable securities and transactions in unlisted entities.

(c) Chapter 3

This Chapter summarises the Advisory Committee's current thinking on other matters raised in the Discussion Paper that may require legislative change. These include strengthening the reporting requirements for directors, amending the test of generally available information and introducing rebuttable presumptions that would apply to senior corporate officers.

(d) Chapter 4

- This Chapter deals with matters raised in the Discussion Paper that the Committee considers should not be changed. These include retaining the existing law that applies to anyone with inside information, whether or not connected with the affected company, and ensuring that informed persons are liable, whether or not they use the information to trade.

(5) Request for comments

- In formulating this Paper, the Advisory Committee has very carefully considered the Submissions on the Discussion Paper. The Committee now invites comments on any matter raised in this Proposals Paper or any other matter relevant to insider trading. All Submissions and comments will be acknowledged in the Final Report.

Please send your comments to:

Mr John Kluver
Executive Director
CAMAC

by any of the following means:

Email: john.kluver@camac.gov.au
Fax: (02) 9911 2955
Post: Corporations and Markets Advisory Committee
GPO Box 3967
Sydney NSW 2001

By hand:

Level 16
60 Margaret Street
Sydney

Closing date for comments:

Please forward your comments by Friday 1 November 2002.

This Proposals Paper is available under What's New on the Advisory Committee's website [http://www.camac.gov.au/](http://www.camac.gov.au/%22%20%5Ct%20%22_new).

(K) FRASER INSTITUTE STUDY: THE ONTARIO SECURITIES COMMISSION SHOULD IMPROVE ITS OWN GOVERNANCE

The Ontario Securities Commission (OSC), a vocal champion of good corporate governance for public companies, may be falling behind its international counterparts in its own governance, says a new study 'The Governance of the Ontario Securities Commission: Lessons from International Comparisons released on 5 September 2002 by The Fraser Institute.

The study compares the governance structure of the OSC with regulators in the US, Australia, UK, and Hong Kong, to explore governance practices that can be adopted by the OSC.

(1) The OSC and international securities regulators

There are similarities in governance between the OSC and modern securities regulators in other countries. These include: requirements for companies to submit annual reports, judicial processes for appealing administrative decisions, and a process of public comment for regulators that have rule-making powers.

But significant differences also exist across the regulators examined in the study. For example, in the United States, extensive use is made of the independent General Accounting Office (GAO) in the oversight of the Securities and Exchange Commission (SEC). In 2001, the GAO released nine different reports, commissioned by Congressional oversight committees, of various aspects of the SEC's operations.

In the UK, while the government has the power to commission similar reviews into the operations of the Financial Services Authority (FSA), operational oversight is primarily undertaken through a statutory non-executive committee composed of the independent board members of the FSA.

In contrast, oversight of the OSC's operations has generally been confined to accounting and financial matters.

(2) Recommendations

There are a number of steps the OSC could take to improve its governance. For example, it could provide more information on its existing governance practices in its annual report, such as what sub-committees of the commission exist and what their functions are. This would enhance the transparency of the OSC's governance.

The Minister of Finance could take a more active role in the OSC's oversight under the existing legislative framework. For example, the minister could take up a 1988 recommendation of the Standing Committee on Government Agencies to ask the Provincial Auditor to undertake an efficiency audit of the OSC. This type of external review helps ensure that a regulator is directing its resources towards its mandated objectives in the most efficient way possible.

Ontario's securities laws are currently being put through a five-year legislative review. The legislative review provides an opportunity to consider more fundamental reforms to the OSC's governance structure. Consideration should be given to restructuring the OSC more along the lines of the UK's FSA so that the non-executive members of its Board are no longer responsible for exercising the OSC's administrative powers.

In such a structure, a regulatory committee operationally independent of both the commission and the OSC's staff would hold the administrative powers. The independent board members could form a committee to report on the OSC's execution of its responsibilities.

The study is available on the Fraser Institute's website at [http://www.fraserinstitute.ca/shared/readmore.asp?sNav=nr&amp;id=477](http://www.fraserinstitute.ca/shared/readmore.asp?sNav=nr&amp;id=477" \t "_new).

(L) AUSTRALIAN LABOR PARTY DIRECTIONS STATEMENT FOR IMPROVING CORPORATE GOVERNANCE

On 29 August 2002 the Hon Senator Stephen Conroy, Shadow Minister for Finance, Small Business and Financial Services released a Directions Statement for improving Australian corporate governance.

Labor's policy commitments include:

- doubling the penalties for serious breaches of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default);
- introducing legislation to protect corporate whistleblowers;
- implementing the recommendations of Professor Ramsay and in addition, banning the provision of certain non-audit services to audit clients;
- requiring auditors to specifically report to shareholders and to a company's audit committee on instances of aggressive accounting;
- requiring auditors to attend and answer questions at annual general meetings;
- requiring the full disclosure of arrangements governing executive remuneration and enforcing the requirements for disclosure in the Corporations Act;
- expensing share options;
- providing to all shareholders any information provided to analysts during an analyst briefing;
- requiring shareholders to be given the following information about candidates for directorships:
. all relationships between the candidates and the company;
. any relationship between the candidate and the directors of the company; and
. any other directorships held by the candidate.
- improve analysts' independence by ensuring that they always act in the interests of the users of the reports - not in the interest of the analyst or the firm which employs the analyst; and
- requiring voting by trustees of superannuation funds supervised under the [Superannuation Industry (Supervision) Act 1993 No. 78 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=6785" \t "default) if the level of voting does not increase to levels comparable with overseas

Further policy options are suggested in the following areas:

- auditor independence and the integrity of financial statements;
- executive remuneration;
- corporate disclosures and information for investors;
- the composition of boards; and
- analyst independence.

The full statement can be obtained from the ALP website at [http://www.alp.org.au/](http://www.alp.org.au/%22%20%5Ct%20%22_new).

(M) CORPORATE SOCIAL RESPONSIBILITY: UNLOCKING THE VALUE

According to a new global survey released by Ernst & Young on 27 August 2002, 94 per cent of companies believe the development of a Corporate Social Responsibility (CSR) strategy can deliver real business benefits, however only 11 per cent have made significant progress in implementing the strategy in their organisation. CEOs are failing to recognise the benefits of implementing Corporate Social Responsibility strategies, despite increased pressure to include ethical, social and environmental issues into their decision-making processes.

Companies identified stakeholder awareness and investor and peer pressures as being key drivers for an increased business focus on developing a CSR strategy.

Research found company CSR programs influence 70 per cent of all consumer purchasing decisions, with many investors and employees also being swayed in their choice of companies. One of the other challenges facing companies implementing a CSR strategy is how to effectively measure its ultimate success via both financial and non-financial indicators.

Senior executives from 147 of the Global 1000 companies from a range of industry sectors throughout Europe, North America and Australasia were interviewed for the survey.

Further information:

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(N) U.S. REGULATORS ISSUE DRAFT WHITE PAPER ON SOUND PRACTICES TO STRENGTHEN THE RESILIENCE OF THE US FINANCIAL SYSTEM

On 22 August 2002, four United States financial services regulatory agencies issued a "Draft White Paper on Sound Practices to Strengthen the Resilience of the US Financial System".

The sound practices identified reflect the preliminary conclusions of the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Securities and Exchange Commission, and the New York State Banking Department regarding the factors necessary to strengthen the resilience of critical US financial markets in the face of a wide-scale, regional disaster. The conclusions are based on recent interviews with industry participants and market utilities about actions being taken to strengthen their ability to recover and resume critical business activities in the event of future wide-scale, regional disruptions. The paper also discusses appropriate timetables for completing reviews and revisions of business continuity plans and implementation of the sound practices.

The sound practices apply most directly to "core clearing and settlement organizations" and "financial institutions that play significant roles in critical markets." Critical markets are defined as the markets for federal funds, foreign exchange, commercial paper, and government, corporate, and mortgage-backed securities.

The agencies request comment on the appropriate scope and application of the sound practices and related issues. After consideration of the comments received, the agencies intend to issue a final version of the White Paper.

Comments are requested by October 21, 2002.

The paper is available on the SEC website at [http://www.sec.gov/](http://www.sec.gov/%22%20%5Ct%20%22_new).

(O) UK FINANCIAL SERVICES AUTHORITY PUBLISHES DISCUSSION PAPER ON HEDGE FUNDS

On 21 August 2002, the UK Financial Services Authority published a Discussion Paper titled 'Hedge Funds and the FSA'. In the Paper the FSA sets out how its regulatory regime bears on the UK activities of hedge funds. The paper asks for comments on:

- the current controls on the selling and marketing of hedge funds in the UK;
- the regulation of UK-based fund managers who manage off-shore hedge funds; and
- the FSA's approach to monitoring the effects of hedge funds on UK markets.

The FSA is seeking views, from industry and consumer groups, on whether it should change the rules on the sale and marketing of hedge funds, to make them more readily accessible. This could potentially increase the product choice available to UK investors. But it also raises significant consumer protection and education issues, which would have to be addressed satisfactorily before any changes were made. In particular, there are legitimate concerns about the comprehensibility to retail investors of the information provided by hedge funds about their activities and risk profiles.

Feedback on the discussion paper is sought by 29 November 2002. The FSA will then publish a feedback statement summarising the views of respondents. Any changes to the regime for authorising hedge funds would be made through the review of Collective Investment Scheme (CIS) regime. The current review of the Listing Rules would take forward any work proposed on listing of hedge funds.

The Discussion Paper is available on the FSA website at [http://www.fsa.gov.uk/](http://www.fsa.gov.uk/%22%20%5Ct%20%22_new).

(P) SEVENTY-FIVE PERCENT OF SENIOR EXECUTIVES EXPECT BOARD OF DIRECTORS WILL BE MORE ASSERTIVE ON KEY ISSUES IN WAKE OF RECENT SCANDALS

PricewaterhouseCoopers' Management Barometer is a quarterly survey of top executives in large, multinational businesses spanning technology; financial services; and consumer & industrial products and services. 145 US CFOs and Managing Directors, and 97 in Western Europe were interviewed in 2002.

Following is a summary of the results of the latest survey.

(1) More board influence expected

According to the survey, 75 percent of executives believe their board generally will be more assertive. Respondents said their board will have more input in the following areas:

- identifying and managing risk - US 57% - Europe 57%
- the company's business structure and transactions - US 55% - Europe 52%
- auditor independence - US 55% - Europe 50%
- the code of conduct - US 47% - Europe 51%
- liquidity issues - US 37% - Europe 34%
- related party transactions - US 36% - Europe 33%
- off-balance-sheet financing - US 33% - Europe 37%
- review of quarterly earnings - US 32% - Europe 39%
- analysts, investors, and the media - US 27% - Europe 38%

(2) Audit committee changes

Executives report that their company has or will make changes in its audit committee in these ways:

- more-frequent audit committee meetings - US 32% - Europe 19%
- longer audit committee meetings - US 31% - Europe 13%
- additional education of audit committee members - US 26% - Europe 17%
- changes in audit committee composition - US 15% - Europe 13%
- changes in the committee's charter - US 15% - Europe 9%

According to Richard Steinberg, US corporate governance leader for PricewaterhouseCoopers "boards in the US meet on average five times a year, about half as often as in Western Europe. Given the number of corporate scandals that have come to light in the US, it seems appropriate that boards of US companies have moved toward more frequent and longer meetings as a means of fulfilling their responsibilities to shareholders".

(3) Value added by the board

Overall, more than 90 percent of executives gave their board good marks for knowledge of the key aspects of the company's business. However, in the US, a majority rated their board as very knowledgeable in just three areas - strategic direction, financial challenges facing the company, and overall performance. In Europe, a majority said their board was very knowledgeable about the company's industry as well.

Senior executives see their board as adding considerable value in the following areas:

- acquisitions, strategic alliances, joint ventures - US 63% - Europe 64%
- corporate strategy - US 56% - Europe 62%
- executive compensation and incentives - US 52% - Europe 45%
- financial reporting - US 50% - Europe 44%
- risk management - US 47% - Europe 50%
- feedback on operating plans - US 47% - Europe 42%

Nearly three-fifths of US respondents (59 percent), and over half in Europe (51 percent) rate their board's advice and counsel to management during times of corporate crisis or economic distress as very or extremely helpful. But ten percent in the US, and eight percent in Europe said the board was not particularly helpful in such situations.

(4) Executive compensation

A majority of US respondents (52 percent), and 43 percent in Europe, view the executive compensation programs set by their board as very or extremely effective for motivating management.

The survey is available on PricewaterhouseCoopers Barometer Surveys website at [http://www.barometersurveys.com/](http://www.barometersurveys.com/%22%20%5Ct%20%22_new).

(Q) INTERNATIONAL FINANCE CORPORATION REPORT CHALLENGES CONVENTIONAL WISDOM ON ROLE OF BUSINESS IN EMERGING MARKETS

A recent report published by the International Finance Corporation (IFC) asserts that it does pay for businesses in emerging markets to pursue a wider role on environmental and social issues.

The business case for sustainability in emerging markets challenges the myth that sustainability is only for rich companies in developed nations, and does not apply to the private sector in the emerging markets. Based on more than 240 real-life examples in over 60 countries, the study analyzes the 'business case' for sustainability in emerging markets - the opportunity for businesses to achieve benefits such as higher sales, reduced costs, lower risks and enhanced reputation from better corporate governance, improved environmental practices, and investments in social and economic development.

Highlighting examples from businesses in Africa, Asia, Central & Eastern Europe, the Middle East and Latin America the report refutes the argument that the business case holds only in developed markets and pinpoints the many opportunities available to diverse businesses. The case studies cover all types of companies, ranging from a small Latvian dairy to an eco-tourism outfit in Peru to an aluminum smelter in Mozambique.

Examining information across six business success factors and seven sustainability factors, the report finds the greatest evidence for business benefits in emerging markets in the areas of cost reductions, productivity, revenue growth and market access. On the sustainability side, environmental process improvements and human resource management represent some of the most significant opportunities for creating value.

The report is the result of collaboration between the International Finance Corporation (IFC), the private sector arm of the World Bank Group; the strategy consultancy SustainAbility; and the Ethos Institute in Brazil.

Copies of the report are available for sale through SustainAbility at [http://www.sustainability.com/store](http://www.sustainability.com/store%22%20%5Ct%20%22_new) or through the World Bank at [http://www.worldbank.org/publications](http://www.worldbank.org/publications%22%20%5Ct%20%22_new).

(R) BROOKINGS INSTITUTE STUDY DETAILS ECONOMIC COST OF RECENT CORPORATE CRISES

The Brookings Institute has released the results of a new study which estimates that the Enron and WorldCom scandals will cost the U.S. economy approximately $37 to $42 billion off Gross Domestic Product (GDP) in the first year.

The study, "The Bigger They Are, The Harder They Fall: An Estimate of the Costs of the Crisis in Corporate Governance," bases its findings on conservative estimates of the effects of the crisis on stock market wealth which are calibrated according to the Federal Reserve Board's model of the U.S. economy.

The authors of the study also describe the likely effect of the corporate governance scandals on other aspects of the economy, including unemployment, inflation, and foreign investment in the United States as well as possible spillover effects beyond U.S. borders. For example, because the crisis has almost certainly discouraged foreign investment into the United States, the result has been a decline in the value of the dollar.

"The Enron and WorldCom bankruptcies resulted from corporate mismanagement and accounting malpractice and symbolize the broader crisis in corporate governance-a crisis that involves top blue chip companies, has reached political leaders at the highest levels of government, and has resulted in high levels of volatility in U.S. stock markets," write the authors. The report concludes with a timeline of significant corporate disclosure breakdowns since the Enron scandal.

The study is available on the Brookings Institute website at
[http://www.brook.edu/views/papers/graham/20020722.htm](http://www.brook.edu/views/papers/graham/20020722.htm%22%20%5Ct%20%22_new)

2. RECENT ASIC DEVELOPMENTS

(A) ASIC RELEASES RAMSAY REPORT ON DISCLOSURE OF FEES AND CHARGES IN MANAGED INVESTMENTS

On 25 September 2002 ASIC released 'Disclosure of fees and charges in managed investments: review of current Australian requirements and options for reform', a report about the disclosure of fees and charges for investment products.

The report was prepared for ASIC by Professor Ian Ramsay, Dean of the Faculty of Law and Director of the Centre for Corporate Law and Securities Regulation at The University of Melbourne.

The report contains:

- an overview of approaches to disclosure of fees and charges in a number of international jurisdictions as well as in Australia; and
- options for improving the quality and comparability of fees and charges disclosure, particularly in Product Disclosure Statements and periodic statements.

The report was compiled after consultation with a cross-section of industry participants and consumer representatives.

'The report is a significant contribution to the current debate about how to take forward the disclosure of investment fees and charges within the Financial Services Reform Act (FSRA) framework', Peter Kell, ASIC's Executive Director, Consumer Protection, said.

'Professor Ramsay's report canvasses a number of disclosure options designed to promote consumer understanding of fees and charges for investment products, and to assist consumers make comparisons between similar products', Mr Kell said.

'The report will facilitate further consultation by ASIC with industry and consumer representatives about the future direction of disclosure for investment products under the FSRA regime', Mr Kell said.

This work is being undertaken with the encouragement of the Parliamentary Secretary to the Treasurer, who has written to industry encouraging their participation.

'It is, however, important to note that while Professor Ramsay's report will assist consideration of disclosure options it does not represent ASIC endorsement of any specific disclosure proposals', Mr Kell said.

ASIC also announced that it will be introducing an investment fees calculator on its consumer website. Introducing such a calculator is one of the report's recommendations and ASIC expects it to be on-line by early next year.

'ASIC's calculator will assist consumers to work out the charges they may incur when considering different investments', said Mr Kell.

The report has been welcomed by the Federal Government, the Labor Party, industry groups and the Australian Consumers' Association.

In a media release dated 25 September 2002, the Association of Superannuation Funds of Australia welcomed the publication of the report and said that it broadly supported the report's recommendations.

The Investment and Financial Services Association, in a media release dated 27 September 2002, has also welcomed the report. IFSA CEO Richard Gilbert commented that "Professor Ramsay has, as we have come to expect over the years, made a significant contribution by adding to the body of knowledge in yet another area of research. The report puts forward many innovative and constructive ideas for better disclosure, in relation to both PDSs and periodic statements".

The report is available from the ASIC website at [http://www.asic.gov.au/](http://www.asic.gov.au/%22%20%5Ct%20%22_new).

Following is summary of the report's recommendations.

The report makes recommendations relating to:

- Improved disclosure and comparability of fees and charges in Product Disclosure Statements (PDS); and
- Improved disclosure and comparability of fees and charges in periodic statements.

Recommendations relating to PDSs

(1) There should be standardised descriptions and definitions of fees including:

(a) all fees to be shown in the one place in PDS (a 'fees section');

(b) disclosure of the purpose of any fees imposed; and

(c) standardised fees table identifying significant fees (eg entry, exit, switching and investment management fees).

(2) There should be separate disclosure of administration fees and investment fees.

(3) There should be improvements in the disclosure of entry/contribution fees and exit/withdrawal fees including:

(a) use of common terminology across all products;

(b) the purpose of these fees should be disclosed (including if used for adviser remuneration).

(4) The capacity to increase fees and maximum fees should be disclosed in the fees section of PDS.

(5) The concept of an ongoing management charge (OMC) should be used as measure of ongoing expenses ('expense measure') across all products (not just superannuation related products) including:

(a) expense measure should not include discretionary fees (eg. entry or exit fees);

(b) standardised description of the expense measure; and

(c) conversion of expense ratio to a dollar amount for an account balance of $10,000 for managed funds (not just superannuation related products).

(6) The effect of fees on returns should be shown over various periods via a table (subject a specified rate of return being set for industry participants and appropriate disclosure of assumptions used).

(7) There should be disclosure in dollar terms, to the maximum extent possible, in addition to showing percentages.

(8) There should be disclosure of fees paid to advisers in fees section of PDS (both for initial investment and on an ongoing basis) including:

(a) showing source of adviser payments (eg. trailing commission comes out of investment management fee); and

(b) disclosure, via a general statement, of the existence of 'soft commissions' and cross-reference to Financial Services Guide (FSG) and Statements of Advice (SoA) for more detail.

(9) There should be standardised descriptions of buy/sell spreads.

(10) The fees section of PDSs should be adjacent to section of PDS which discloses returns.

(11) There should be standardised disclosure of ability to negotiate rebates with advisers (eg. statement that adviser can determine amount of entry fee).

Recommendations related to periodic statements

There should be disclosure of actual fees relating to a person's investment (where this can be calculated) subject to ASIC obtaining information from industry about the costs of providing this sort of disclosure or, alternatively, disclosure of an indicative amount (either an amount determined by multiplying a fund's per share (unit) asset value by the fund's expense ratio and then by the average number of shares (units) a person owned during the reporting period OR a dollar amount based on a fund's actual expenses of a standardised investment amount (eg $10,000) assuming a standardised return (eg 5%).

(B) ASIC AMENDS POLICY ON SHARE PURCHASE PLANS

On 18 September 2002 ASIC announced changes to its policy for share purchase plans contained in ASIC Policy Statement 125: Small offers of shares to existing shareholders by listed companies - share purchase plans [PS 125].

These changes were made following submissions by various shareholder and industry groups.

In brief, the amendments made to ASIC's policy are:

- the yearly limit that can be raised under ASIC's policy will be increased from $3000 to $5000 for each eligible participant. This change has been made to take into account increases in the Consumer Price Index and changes in market participation since the Class Order was first released in 1998;
- a clarification of who can receive offers under the relief. The relief will make it clear that a trustee or nominee expressly noted on a company or scheme register may receive an offer for each occasion they are separately recorded as a trustee or nominee for a different beneficiary named on that register; and
- extension of the relief to registered managed investment schemes listed on the Australian Stock Exchange Limited (ASX).

The changes in policy are consistent with ASIC's policy rationale to allow share purchase plans when:

- the risk to the investor is limited because the amount which may be invested by each investor per annum in the scheme is restricted; and
- the benefits to investors (such as savings on brokerage) outweigh the disadvantages and risks of not having full prospectus disclosure.

These changes will assist shareholders and industry to participate in more cost-effective fundraising without unduly compromising investor protection.

ASIC considers any further expansion of its policy in this area is more appropriately an issue to be dealt with by law reform.

A share purchase plan is a plan for the offer of shares by a corporation listed on the ASX, where ASIC will give relief so that they can offer existing shareholders the opportunity to acquire small numbers of additional shares without the benefit of a disclosure document or Product Disclosure Statement (PDS).

The class orders which give effect to the changes to ASIC's policy are:

- Class Order [CO 02/831], which provides disclosure relief for securities;
- Class Order [CO 02/832], which provides disclosure relief for managed investment products from Part 7.9 of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default); and
- Class Order [CO 02/991], which varies Class Order [CO 98/52]. It gives relief from some of the managed investment provisions for purchase plans made available by some responsible entities.

ASIC plans to make consequential changes to PS 125 before the end of this year.

Copies of the amended Class Orders are available from the ASIC website at [http://www.asic.gov.au/](http://www.asic.gov.au/%22%20%5Ct%20%22_new), or by calling Infoline on 1300 300 630.

For further information contact:

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(C) ASIC ISSUES NEW CLASS ORDERS ABOUT WARRANTS

On 17 September 2002 ASIC issued new Class Orders covering takeovers and substantial holdings warrants.

The new Class Orders contain technical changes that take into account legislative amendments and some developments in warrant products, particularly 'instalment' and 'endowment' warrants.

The new Class Orders issued to replace the existing Class Orders are as follows:

- Class Order 02/929 [CO 02/924] replaces [CO 00/451];
- [CO 02/925] replaces [CO 00/452];
- [CO 02/926] replaces [CO 00/453]; and
- [CO 02/927] replaces [CO 00/454].

(1) Call warrant holders CO 02/924

Currently, under section 609(6)(b) of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default), a person docs not have a relevant interest merely because they have a right to acquire the securities given by a derivative. ASIC is continuing to provide relief for holders because some warrants may be securities rather than derivatives.

Additionally, section 609(6)(b) only applies to a relevant interest that the holder has because of their right to acquire the securities. Without relief, the holder may have a relevant interest because of any right under the warrant to require the securities be kept in trust.

While as a result of the relief, no relevant interest arises for the purposes of the takeover provisions (Chapter 6) as a consequence of holding a call warrant, any interest that would arise but for the relief, is taken into account for the purposes of the substantial holding provisions (Chapter 6C). This is consistent with the treatment of derivatives under the definition of 'substantial holding' in section 9 and section 671B(7).

(2) Association CO 02/925 and CO 02/926

The new Class Orders take account of the new definition of 'associate' in s12 of the Corporations Act as amended by the [Financial Services Reform Act 2001 No. 122 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=58127" \t "default). For certainty, they give relief to disregard any association between warrant issuers and warrant holders merely because or the warrant.

(3) Put warrant issuers CO 02/926

A warrant issuer may have a relevant interest in the underlying security because the holder, under the terns of the warrant (or the trust securing obligations under the warrant), has given the issuer a right in relation to the securities.

In particular, this may arise in relation to instalment or endowment warrants with a loan component. Under such a warrant, the holder may be required to place the underlying security in trust to secure their obligations, Without relief, the issuer may have a relevant interest because of section 608(8)(b)(ii) of the Corporations Act, as the issuer has a right to dispose of the securities held in trust if the holder does not exercise the put option.

Former Class Order 00/453 only dealt with the issuer's relevant interest arising under section 608(8)(b)(ii) as a result of the put option.

(4) Warrant trustees CO 02/927

CO 00/454 gave takeover and substantial holding relief to a trustee that holds shares as cover under a warrant trust deed. It only applied to the trustee's discretions dealing with insolvency or default of the issuer or holder.

The new Class Order recognises that the purpose of the trust may be to secure the obligations of the warrant holder under the warrant as well as the warrant issuer.

It recognises that under the terms of the warrant, a trustee may exercise a range of discretionary powers over securities in trust. It is unlikely these powers would be used as a means of gaining control of a company.

It also addresses additional matters, including:

- discretions in relation to transactions affecting share capital, such as rights issues or capital reconstructions;
- discretions in relation to takeover bids or schemes of arrangement (the relief allows for a discretion to bring forward the time for exercise but not a discretion to decide whether to accept or reject a bid); and
- discretions to lend the securities.

(5) Second option contained in warrant

Some instalment and endowment warrant products contain a second option. For example, a covered call warrant may also allow the holder to put the shares to the issuer in certain circumstances and receive a cash payment. Relief for put warrants applies to such products as well as relief for call warrants.

(6) Policy Statement 143 Takeover Provisions: Warrants

ASIC will continue to apply the broad principles set out in Policy Statement 143 Takeover Provisions: Warrants when assessing the appropriate regulatory treatment of particular warrant products.

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(D) COLES MYER - ASIC CALLS FOR MORE INFORMATION AND SHAREHOLDER ACTIVISM

In a media released dated 16 September 2002, Mr David Knott, Chairman of ASIC emphasised the importance of restoring long-term stability to Coles Myer Limited's governance structure.

'The current instability at Coles Myer is a serious cause of confusion and concern. It appears increasingly likely that shareholders will be required to make important decisions at the November annual general meeting affecting the composition of the Board and the future direction of the company', Mr Knott said.

'In order for them to do so, they need to be fully informed of the contested issues and of any differences in strategic direction being advocated for Coles Myer by relevant directors or shareholders. The current level of publicly available information about all of these matters is inadequate', he said.

ASIC is also calling on all shareholders of Coles Myer to inform themselves of the issues at stake ahead of the annual general meeting and to exercise their votes in person or by proxy.

'The widespread shareholding register of Coles Myer will empower retail shareholders to strongly influence the outcomes at the annual general meeting. They need to take an active role in ensuring that the performance of their company is not undermined by prolonged instability at Board level', said Mr Knott.

Mr Knott also drew attention to ASIC's class order designed to ensure that institutional investors are able to discuss and agree in advance of such meetings about how they will vote on corporate governance issues.

Policy Statement 128: Collective Action by Institutional Investors provides relief from the provisions of Chapter 6 of the [Corporations Act 2001 No. 122 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default), which may otherwise prohibit large institutional shareholders, whose collective votes exceed 20 per cent of the voting power in a company, from agreeing in advance on how to vote on issues such as the election or removal of directors.

'ASIC recognises that issues of governance are generally in the hands of the Board and shareholders. However, there are serious implications for the broader market when major divisions appear at Board level of a large listed company. For that reason, ASIC will closely monitor the Coles Myer situation in the period leading up to the annual general meeting in November', said Mr Knott.

(E) OVER 100 PRODUCT DISCLOSURE STATEMENTS LODGED WITH ASIC SINCE INTRODUCTION OF FSRA

On 16 September 2002 ASIC announced that more than 100 Product Disclosure Statements (PDS) in-use notices have been lodged with ASIC since the introduction of the [Financial Services Reform Act 2001 No. 122 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=58127" \t "default) (FSRA) on 11 March 2002.

ASIC has also announced the results of its regular monitoring and enforcement program in relation to the PDS requirements under the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482).

A PDS is the point-of-sale document that sets out the significant features of a financial product, including its risks, benefits and costs, and applies to all products issued since the FSRA commenced on 11 March 2002. It is designed to help consumers compare and make informed choices about financial products.

In general, under the Corporations Act (as amended by FSRA), a retail client must receive a PDS before acquiring a financial product, including managed investments, superannuation products, insurance products, retirement savings accounts, deposit products and derivatives.

In the first six months since the new PDS regime commenced, 102 PDS in-use notices (Form FS53) have been lodged with ASIC, which cover the following product types:

Managed Investment (38)
Superannuation (excluding SMSF) (6)
Life Risk Insurance (8)
Investment Life Insurance (5)
Derivatives (7)
Self Managed Super Funds (37)
General Insurance (1)
Total (102)
11 March to 5 September 2002

As part of its general compliance program, ASIC selected 45 of these PDS documents for review. As a result of deficiencies identified in a number of these documents, ASIC has issued four interim stop orders and one final stop order, and accepted two supplementary, and one replacement PDS document.

(1) Mediterranean Olives Estate Limited

ASIC placed a final stop order on the PDS document issued by Mediterranean Olives Estate Limited due to concerns it did not include updated information on the status of the tax product disclosure ruling, in contravention of the Corporations Act. It also failed to support material assumptions underpinning prospective financial information. The final
stop order was issued following a hearing.

ASIC also placed an interim stop order on the PDS documents of Environinvest Limited, the New World RE Ltd forestry plantation, and the Heydon Park Limited ginseng project.

(2) Environinvest Limited

ASIC was concerned that the original PDS did not clarify the fees to be charged to investors and clauses in material agreements, and that the information provided to investors was not set out in a clear and concise matter, as required under the law.

Environinvest has subsequently issued a supplementary PDS, dated 29 August 2002, addressing ASIC's concerns. The interim stop order has now been lifted.

(3) Heydon Park Limited

ASIC placed an interim stop order on the Heydon Park Limited PDS due to a lack of disclosure in relation to let out clauses in a fixed contract for the sale of the product, other assumptions that formed the basis of the financial forecasts, and the financial strength of the purchaser. Heydon Park Limited has now issued a supplementary PDS that provides additional disclosure in relation to these issues, resulting in the lifting of the interim stop order.

(4) New World RE Ltd

An interim stop order was issued on the PDS of New World RE Ltd, because it failed to accompany headlined rates of return with prominently displayed references assumptions. It also failed to provide sufficient evidence to demonstrate reasonable grounds for including prospective financial information, including the inflation rate, predictions on costs and stumpage prices, and did not specify the species of trees to be planted.

New World RE Ltd has agreed to issue a replacement PDS to deal with these issues.

'Product issuers are responsible for ensuring that a PDS meets the PDS requirements, and that information is presented clearly, concisely and effectively', said ASIC Director Financial Services Regulation, Mr Sean Hughes.

'In general, ASIC will not vet any PDS prior to its release to consumers, and will take appropriate remedial action to ensure consumers' interests are protected', he said.

Further information about PDS's can be obtained from the ASIC website at ([http://www.asic.gov.au/](http://www.asic.gov.au/%22%20%5Ct%20%22_new)), or Policy Statement 168 -Disclosure: Product Disclosure Statements (and other disclosure obligations).

For further information contact:

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(F) HIGH COURT REFUSES SPECIAL LEAVE IN YANDAL MATTER

On 13 September 2002 Mr David Knott, Chairman of ASIC welcomed the decision of the High Court to refuse an application for special leave to appeal the decision of the Federal Court in the Yandal litigation.

ASIC commenced the litigation in March 1933 to protect the interests of shareholders it believed were disadvantaged by the takeover of Great Central Mines Ltd in early 1999.

As all avenues of appeal have been exhausted, shareholders who accepted the bid for Great Central Mines are now assured of receiving the $28.5 million compensation ordered by Justice Merkel, as well as interest accrued since June 1999', Mr Knott said.

'Given the lapse of time since Justice Merkel made this order, the parties will need to return to the Federal Court for further directions on the formal process for offering shareholders their withdrawal rights, and the subsequent distribution of money. ASIC is hopeful that all necessary directions and administrative requirements can be finalised in time for compensation payments to be mailed to relevant shareholders within the next three months', Mr Knott said.

(1) Background

In June 1999, Justice Merkel found that Yandal Gold Pty Ltd, Edensor Nominees Pty Ltd (the trustee of the Gutnick Family Trust) and subsidiaries of Normandy Mining Ltd, breached the takeover provisions of the Corporations Law in relation to the takeover of Great Central Mines Ltd.

Justice Merkel found that the contraventions 'enabled the Normandy group and Edensor using Yandal Gold as the bid vehicle, to make a highly successful takeover bid for Great Central Mines shares at a significantly lower price than would have had to be paid at that time had the bid proceeded without the unlawful "agreements" which secured Edensor's "support" and contravened section 615'.

Justice Merkel found that these arrangements 'resulted in a significant detriment to shareholders', and ordered that:

- Edensor Nominees pay $28.5 million (plus interest) to shareholders who had accepted into the bid for Great Central Mines and not withdrawn their acceptance; and
- each person who accepted the offer by Yandal Gold or had their shares compulsorily acquired, be entitled to withdraw their acceptance and return any money paid for their shares to Yandal Gold.

ASIC commenced the action after becoming concerned that the Great Central Mines takeover was not occurring in an informed and efficient market.

Edensor appealed Justice Merkel's decision to the Full Federal Court, which found in March 2000 that Justice Merkel's order that Edensor pay $28.5 million was invalid for want of jurisdiction, and that the Federal Court had no jurisdiction to hear and determine the proceedings under the Corporations Law.

ASIC successfully appealed that decision to the High Court which subsequently ordered in August 2000 that the Full Federal Court orders regarding jurisdiction be set aside and that the matter be sent back to the Full Federal Court.

The matter then returned to the Full Federal Court for a decision on the merits of the balance of Edensor's appeal.

In March 2002, the Full Federal Court upheld Mr Justice Merkel's orders.

Endensor then sought special leave to the High Court to appeal the Full Federal Court's decision. It was this application that was refused on 13 September 2002.

Edensor was ordered to pay ASIC's costs of the special leave application.

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(G) SIMON HANNES FOUND GUILTY

On 11 September 2002 Mr Simon Gautier Hannes, a former executive director of Macquarie Bank Limited, was convicted on one charge of insider trading in the securities of TNT Limited (TNT) and two charges under the [Financial Transaction Reports Act 1988 No. 64 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=6635" \t "default).

The conviction of Mr Hannes follows a 15-week retrial in the Supreme Court of New South Wales, which was prosecuted by the Commonwealth Director of Public Prosecutions.

Mr Hannes was originally convicted on the same charges in the Sydney District Court in August 1999 and was jailed for two years and two months and fined $110,000.

However, the convictions were quashed following a decision by the New South Wales Court of Criminal Appeal in December 2000, and he was released after serving 15 and a half months of the sentence. The convictions are the result of a retrial.

The insider trading charge related to Mr Hannes, using the name 'Mark Booth', acquiring 5,000 TNT $2 call options in September 1996 through Ord Minnett Limited, when he had knowledge that TNT was likely to be the subject of a takeover bid.

The ASIC investigation of 'Mark Booth's' trading started within 24 hours of the announcement of a takeover by Dutch company Royal PTT Nederland NV (KPN) at $2.45 on 2 October 1996.

Within two days, ASIC obtained court orders freezing the $2 million profit from 'Mark Booth's' trading, and this profit was ultimately returned to the people who had sold the call options.

ASIC's investigation into the circumstances surrounding 'Mark Booth's' purchase of call options was conducted in collaboration with the Australian Federal Police and the Australian Stock Exchange. ASIC was able to identify Mr Hannes as the person who had bought the TNT $2.00 call options.

The Financial Transactions Reports Act charges relate to Mr Hannes making six cash withdrawals in one day from different bank branches and then using the cash to acquire 9 bank cheques, again from various banks and branches, with a view to avoiding the reporting requirements under the Act.

Mr Hannes, who remains on bail, will appear for sentencing on 7 November 2002.

(H) ASIC CONCLUDES INVESTMENT FUNDS PROJECT, GIVES TAKEOVER RELIEF TO INDEX FUNDS

On 11 September 2002 ASIC announced that it would not give broad relief from the takeover regime to investment funds, but may give a case-by-case exemption to index funds.

ASIC reached this decision after considering the submissions received in response to the discussion paper 'Investment funds: takeovers and substantial holding relief' issued in November 2001.

The discussion paper sought comments on proposals that the current legislative settings for takeovers and disclosure by substantial security holders disadvantaged members of public investment funds.

The discussion paper canvassed options including no change, ASIC exemptions or legislative change. While the majority of submissions opposed broader relief from the takeover regime, ASIC received submissions in both support and opposition.

ASIC has referred its findings to Treasury so that the issues raised in response to the discussion paper may be considered as part of any future review of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) takeover provisions.

(1) Index funds

ASIC may give a case-by-case exemption from the takeovers prohibition (section 606) for index funds within financial services groups, on the basis that an index fund has a limited discretion in the acquisition and disposal of securities.

Index funds invest in a portfolio of securities and are a designed in such a way that their value tracks a nominated market index.

ASIC does not believe that an index fund should be compelled to refuse further subscriptions, or increase its tracking error, merely because group holdings in a company represented in the index are close to the 20 per cent takeover threshold.

ASIC will impose conditions to ensure that to qualify for the relief an index fund closely tracks the index. Relief will be made on the condition that an index fund does not vote shares held by the fund.

At this stage, the index fund relief will 'sunset' after two years. ASIC will assess the operation of a fund's relief before granting or denying a further extension.

The relief for index funds does not extend to the substantial holding provisions.

(2) Requirements applying to index funds relief

Requirements for index funds applying for exemption from section 606 include that:

- the offer document or investment mandate of a fund states an objective to maintain a tracking error of less than 0.5 per cent per annum, and the fund maintains systems and processes which give a reasonable assurance that the tracking error will be maintained;
- the index fund's holding in shares in a company is not more than 5 per cent over the company's index weighting in the relevant index;
- an independent third party must review compliance with the tracking error requirements every six months;
- the index fund does not vote shares held in the fund, unless this takes place in accordance with a direction by a client under a client mandate agreement; and
- after 18 months, the fund must provide ASIC with a report on the practical operation of the exemption, including details of voting shares acquired in reliance on the exemption.

(I) PROSPECTIVE FINANCIAL INFORMATION

On 6 September 2002 ASIC released a final policy statement on the use of prospective financial information, including financial forecasts, in prospectuses, disclosure documents and product disclosure statements.

The final policy statement contains expanded guidance in particular areas, including an outline of what is not considered reasonable grounds for prospective financial information, and what ASIC expects of an expert who prepares a report for a disclosure document.

ASIC notes that in addition to its policy statement, further guidance for independent accountants has also been recently released. AGS 1062 'Reporting in Connection with Proposed Fundraisings' is available through [another website] [http://www.aarf.asn.au/](http://www.aarf.asn.au/%22%20%5Ct%20%22_new).

Copies of Policy Statement 170 can be obtained by logging on to ASIC's website at [http://www.asic.gov.au/](http://www.asic.gov.au/%22%20%5Ct%20%22_new) or by calling ASIC's Infoline on 1300 300 630.

(J) DISCUSSION PAPER ON ADMINISTRATION OBLIGATIONS

On 5 September 2002 ASIC released a discussion paper about the financial reporting and annual meeting obligations of companies under administration or subject to a deed of company arrangement.

'ASIC believes that the appointment of an external administrator does not remove the obligation on a company to prepare and lodge its financial reports. Many companies do not appear to be aware of this obligation when they go into external administration', ASIC Director, Corporate Finance, Richard Cockburn said.

'This paper reminds administrators and companies, that their obligations to prepare financial reports do not cease or become suspended as a result of the administration.'

'It also emphasises that ASIC can give relief from these obligations where it is appropriate. In crafting relief, we will consider how best to protect the interests of members and other parties in financial information about a company in administration yet recognise the priority tasks for administrators', he said.

ASIC has issued a class order giving interim relief during the consultation period. The relief provides many companies in external administration with a moratorium from any upcoming requirement to prepare and lodge a financial report. The class order is published on the ASIC website.

However, companies should be aware that this class order does not extend to holding a company's Annual General Meeting (AGM). Companies seeking an extension to hold their AGM will still need to make an individual application to ASIC in the usual manner.

ASIC is seeking public comment on the proposals in the paper by 31 October 2002.

(K) ASIC GIVES INTERIM LICENSING RELIEF FOR OPERATORS OF POOLED DEVELOPMENT FUNDS

On 2 September 2002 ASIC released a new Class Order giving interim relief to operators of pooled development funds (PDF operators) from the Australian financial services licensing requirements in the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default).

The new Class Order [CO 02/0930] enables PDF operators to raise capital (ie. issue securities of the PDF) without having to be licensed under the Act.

The relief applies for a period of 12 months from 17 August 2002 until 17 August 2003. The relief only applies in relation to a PDF that is registered under the [Pooled Development Funds Act 1992 No. 100 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=6648" \t "default), and where the PDF operator:

- has entered into an enforceable contract with a third party licensee (including a licensee under the old Act during the transition for the financial services reforms), for the purpose of administering its investments, under which it obtains financial product advice;
- issues securities of the PDF to wholesale clients, as defined in s761G(4) of the Act;
- offers to issue securities of the PDF are made under an offer document that does not contain any personal advice, as defined in s766B(3) of the Act; and
- does not carry on any other financial service, such as providing financial product advice.

ASIC will provide this relief for a period of 12 months only to allow the PDF industry sufficient time to have their case for a permanent licensing exemption considered by Treasury. ASIC's interim relief should not be construed as a recognition of the merits of any industry submission.

ASIC is aware that some PDF operators may not be able to meet the requirements of the new class order relief.

Therefore, in addition to the class order relief, ASIC will continue its current general no-action position relating to the licensing of PDF operators for a similar period of 12 months from 17 August 2002 until 17 August 2003.

PDF operators relying on ASIC's no-action position should note that while ASIC will not enforce the licensing requirements against them during this 12 month period, third parties may still be able to take action to enforce provisions of the Act against PDF operators. A copy of Class Order [02/0930] can be obtained from the ASIC's Infoline on 1300 300 630, or from the ASIC website at [http://www.asic.gov.au/](http://www.asic.gov.au/%22%20%5Ct%20%22_new).

3. RECENT TAKEOVERS PANEL MATTERS

(A) PANEL DECISION IN RELATION TO COLONIAL FIRST STATE PROPERTY TRUST GROUP

On 12 September 2002 the Takeovers Panel advised that it had accepted undertakings in relation to the proposal (Merger Proposal) for the merger of Colonial First State Property Trust Group (Colonial Funds) with the Commonwealth Property Office Fund (Commonwealth Fund) and the Gandel Retail Trust (Gandel Fund). On the basis of the undertakings the Panel has decided not to make a declaration of unacceptable circumstances in response to applications by Mirvac Funds Ltd. (Mirvac) as the responsible entity for Mirvac Property Trust (Mirvac Fund) made on 29 August and 2 September 2002.

The Panel received submissions from ASIC and the responsible entities of the funds.

The Panel received undertakings from:

(a) CFS Managed Property Ltd (CFS) the Responsible Entity for the Colonial Fund; and

(b) those associates of both Commonwealth Bank of Australia (CBA), and the Gandel Group of companies, which are unitholders in the Colonial Funds and which owe either statutory or fiduciary duties to the persons on whose behalf they hold or control the units (Associated Unitholders).

The undertakings from CFS relate to disclosure issues in the notice of meeting for the meetings proposed to be held in the Colonial Funds to consider the Merger Proposal (Meetings).

The undertakings from the Associated Unitholders affirm their obligations to act in the best interests of the persons on whose behalf they hold or control the units, given the potential for conflict of interest that the related nature of the various fund management entities in the Merger Proposal generates.

One associate of the Gandel Group is a small unitholder in one of the Colonial Funds. It has undertaken not to vote at the Meetings.

(1) Mechanism

The Panel does not accept the proposition put forward by Mirvac that the Merger Proposal (of the Colonial Funds with the Commonwealth and Gandel Funds) should not proceed by way of resolutions under section 601GC and Item 7 of section 611 of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482). It also advises that it considers that the Merger Proposal as formulated had deficiencies, which have been dealt with by the undertakings.

(2) Disclosure

The Panel considers that there are some material deficiencies in the explanatory statement accompanying the notice of meeting (Explanatory Statement) which was sent to the unitholders in the Colonial Funds. Accordingly, the Panel invited CFS to undertake to send a supplementary notice to unitholders in the Colonial Funds setting out, as a minimum, the following issues:

- Full disclosure of the relationship to CBA and the Gandel Group of the Associated Unitholders (to the extent known by CFS);

- A statement concerning the undertakings made by the Associated Unitholders referred to above;

- A statement clarifying the effect of the liability disclaimers made in the Explanatory Statement dated 30 July 2002, and disclosing clearly that such purported disclaimers do not reduce any statutory liability imposed under the Corporations Act in relation to misleading and deceptive conduct, and clearly explaining the limit of the effect of the disclaimers;

- The effects on the amount of management fees that are likely to be payable to the Responsible Entity of the Commonwealth Fund and Gandel Fund in the event that the Merger Proposal is approved, and the relationship of the Commonwealth and Colonial Responsible Entities with each other and with CBA. CFS has undertaken to do this by providing examples based on the new fees and how they would have applied for the year ending 30 June 2002 if the funds had been merged throughout that year; and

- A full explanation of the effect of all changes to the fees and charges of the Responsible Entities of the two ongoing trusts if the Merger Proposal proceeds, taking into account all changes announced on or before the date of the supplementary notice.

(a) Directors' recommendation

The Panel considers that the directors of CFS (Colonial Directors) should provide an updated recommendation in the supplementary material which the Panel has required CFS to provide to unitholders in the Colonial Funds, similar to the recommendations and reasons which would have had to have been given by the Colonial Directors if the Merger Proposal had been undertaken by way of a takeover bid. The Panel also considers that the Colonial Directors should provide their reasons for such recommendation. CFS has undertaken to do so.

(b) Sending the information

CFS has undertaken to post the additional information to unitholders in the Colonial Funds at least ten days before the date of the Meetings. It has also undertaken to give a copy of the additional disclosures, referred to above, to Mirvac at least 12 hours before printing.

(c) BDO Report

Mirvac requested that the Colonial Directors instruct BDO Corporate Finance P/L (BDO) to provide a fully revised report to the Colonial Fund unitholders on the fairness and reasonableness of the Merger Proposal. It submitted that this was necessary in light of the takeover offer for the Colonial Funds announced by Mirvac and the subsequent variations to both the Merger Proposal and the Mirvac bid. Mirvac noted that thus far BDO has only been instructed by the Colonial Directors to prepare a restricted review of its conclusion and opinion.

The Panel does not consider it appropriate to require the Colonial Directors to instruct BDO in this way. The Panel considers that it is currently fully within the discretion of the Colonial Directors to choose whether or not to do so.

The Colonial Directors, in their initial recommendation stated that their recommendation was supported by the conclusions of BDO. The weight which the Colonial Directors will be able to place on BDO's conclusion in any future recommendation to unitholders in the Colonial Funds will clearly depend on the currency and breadth of any then existing report by BDO. On that basis, the Colonial Directors should not make any recommendation that is stronger than the then currently updated report would allow, if they wish to base or support their recommendation on that independent report.

(3) Proxies

Mirvac requested that all proxies for the Meetings should be determined to be invalid because of the passage of time and volume of new information since they were lodged. The Panel does not accept this.

However, the Panel considers that CFS should, in its supplementary notice of meeting, provide fresh proxy forms to all unitholders in the Colonial Funds. CFS has also undertaken to advise unitholders who have already lodged proxies that they should consider their proxies in light of the supplementary disclosure, and that lodging a fresh proxy will automatically revoke any earlier proxy, and that attending the Meetings will suspend the authority of a proxy to speak and vote for that unitholder.

(4) Voting

The Panel considers that Associated Unitholders should not be excluded from voting (or from having their votes taken into account) where those associates have a fiduciary duty to persons other than the CBA or the Gandel Group of companies. Their voting is subject to the requirement in section 253E of the Act that any person who is an associate of the Responsible Entity and has an interest other than as a unitholder may not vote. The Associated Unitholders have given the required undertakings.

The Panel will also require a record of the voting on the resolutions to be kept and a summary of that record to be included in the notice of resolution lodged with ASIC.

(5) Process

The Panel came to its preliminary decision on Friday 6 September and advised the parties that evening. At that time it offered the parties an opportunity to resolve the issues by way of providing undertakings to the Panel. The last of these undertakings was provided on 12 September.

The Panel has encouraged any steps which CFS might take to arrange the timing and distribution of the additional material to unitholders in the Colonial Funds in a way that assists them to deal with the large volume of information that they will be receiving from CFS, and from the Commonwealth, Gandel and Mirvac funds.

(6) Future policy /precedent value of this decision

The Panel notes that the issues raised in this application go to some fundamental questions as to the mechanism of mergers of Managed Investment Schemes by "Schemes of Arrangement". The Panel considers that these issues should be considered in a broader context than simply the facts of this application, and that the process of consideration should be open to public consultation. Accordingly, it will forward these issues to a joint working group from ASIC and the Panel to develop appropriate policy in this area. That public policy process, combined with the special facts of this matter, will very likely limit the value of this decision as precedent.

The sitting Panel for the application was Professor Ian Ramsay (sitting President), Karen Wood (sitting Deputy President) and Jennifer Seabrook.

(B) PANEL DECISION IN RELATION TO ONLINE ADVANTAGE LIMITED

On 10 September 2002 the Takeovers Panel advised its decision in relation to applications made by McWilliam Nominees Pty Ltd and ASIC in relation to the affairs of Online Advantage Limited.

On 4 July 2002, McWilliam Nominees lodged an application for a declaration of unacceptable circumstances under Section 657A of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) in relation to the alleged acquisition by certain persons specified in the application of approximately 100 million shares in Online Advantage on or around 3 June 2002 ("3 June Crossing").

On 1 August 2002, ASIC made an application in relation to Online Advantage also seeking a declaration of unacceptable circumstances in relation to the same events as the original application by McWilliam Nominees.

The Panel has received submissions from all interested parties in relation to the matter and has conducted conferences with all those parties it considered relevant to the proceedings. It has further conducted its own investigation in respect of all relevant documentation relating to the matter.

After due consideration of all of the matters surrounding the 3 June Crossing, the Panel has accepted undertakings from Online Advantage, Euroz Securities and Shaw Stockbroking. Under the undertakings, Online Advantage will make an offer of a selective buy-back of shares at 3.1c per share to those shareholders who acquired their shares in Online Advantage prior to 3 June 2002, and who remain shareholders of Online Advantage at the time that buy-back offers are made and accepted ("Relevant Shareholders"). Online Advantage will conduct the buy-back in accordance with the relevant provisions of Part 2J.1 of the Corporations Act and will, if required, seek shareholder approval for the buyback at the next annual general meeting of Online Advantage (which will be held on or before 30 November 2002).

The appointments of all directors of Online Advantage will expire at that AGM.

Online Advantage has provided an undertaking to the Panel to disclose in the share buy-back offers and in the notice of meeting to be sent to shareholders all benefits given, or which have been agreed to be given, by Online Advantage to related parties of the company and entities which are related to, or otherwise connected with, any director of the company.

In this regard, the Panel notes that Online Advantage and Churchill Capital Pty Ltd (an entity associated with Karl Paganin and Patrick O'Connor, two of the directors of Online Advantage) have entered into an agreement pursuant to which Churchill will provide all management and other services to Online Advantage. On that basis, Online Advantage and the Panel have agreed that it would be appropriate to provide shareholders of Online Advantage with information on those arrangements. Therefore, Online Advantage and Churchill have agreed that Online Advantage will set out, in the share buy-back offers and in the notice of meeting for the AGM, details of payments to, and contracts with, Churchill and related entities and to its or their employees.

Online Advantage has undertaken to provide similar information for each director who stands for election, and advice of the top 20 shareholders in Online Advantage and the relationships and connections which shareholders would reasonably expect to know in assessing the ownership of the company.

If the necessary consent or approval for the buy-back is not obtained, Shaw Stockbroking and Euroz Securities have agreed to underwrite the sale of the shares by the Relevant Shareholders who otherwise wish to accept the buy-back offer. Shaw Stockbroking and Euroz Securities advise the Panel that they believe that their agreement to underwrite this sale is a reasonable commercial resolution of the matter, but have stressed that this in no way implies any wrongdoing on their part.

The Panel is of the view that the undertaking it has received from Online Advantage, Shaw Stockbroking and Euroz Securities adequately address the Panel's concerns in relation to the 3 June Crossing. They provide an arrangement whereby the Relevant Shareholders who no longer wish to be shareholders of Online Advantage have a reasonable and equal opportunity to dispose of their shareholding. That opportunity will be at the same price as offered to the shareholders who sold their shares in the 3 June Crossings and a further crossing of 19.9% of the shares in Online Advantage which occurred on 16 July 2002.

As a result of the above arrangement, the Panel has declined to make a declaration of unacceptable circumstances and has terminated the interim orders.

The Sitting Panel for this application was constituted by Braddon Jolley (sitting President), Brett Heading and Chris Photakis.

(C) PANEL RELEASES FINAL GUIDANCE ON CONFLICTS OF INTEREST

On 30 August 2002 the Takeovers Panel advised that it had released a Guidance Note on conflicts of interest as they relate to Panel members sitting on individual matters. The final version follows public consultation on a draft that the Panel released in June 2002.

The final Guidance Note is based on the Panel's underlying policy that:

- in the interests of maintaining transparency of process, all material relevant interests of a member of which the President of the Panel becomes aware will be disclosed to the parties to proceedings, even if the interests are not sufficiently direct to give rise to a conflict;
- members are asked to consider any material personal and professional interests that may give rise to a conflict. In respect of professional interests, members are asked to conduct all inquiries which are reasonable in the circumstances to determine whether they have any material interest which gives rise to a conflict, or which should be disclosed to the parties;
and
- in order to facilitate the speedy appointment of a sitting Panel, the Panel regards it as important that applicants provide, at the time of their application, information which will assist members to conduct conflict inquiries. For the same reasons, the Panel regards it as important that parties discuss with the Panel Executive, as early as possible, any potential conflicts of which they are aware, of in respect of which they have concerns.

The Panel has also published on the Panel's website a paper that provides details of the Conflicts Sub-Committee's response to external comments on the consultation draft. That paper is under the "Consultation" tab on the Panel's website.

The Panel appreciates the time that its members give to it on a number of guidance notes and other projects. The Panel and the Panel Executive wish to thank the Conflicts Sub-Committee for their work on this Guidance Note.

The Conflicts Sub-Committee comprised Ms Alison Lansley, Ms Alice McCleary and Professor Ian Ramsay.

The Conflicts Guidance Note and the Public Consultation Response are available at:
[http://www.takeovers.gov.au/Content/guidance/conflicts\_draft.asp](http://www.takeovers.gov.au/Content/guidance/conflicts_draft.asp%22%20%5Ct%20%22_new)
[http://www.takeovers.gov.au/Content/consultation/conflicts.asp](http://www.takeovers.gov.au/Content/consultation/conflicts.asp%22%20%5Ct%20%22_new)

4. RECENT CORPORATE LAW DECISIONS

(A) WHETHER CERTAIN RESOLUTIONS PROPOSED BY MEMBERS SHOULD BE DECLARED TO BE INVALID
(By Emma Bloomer, Phillips Fox)

National Roads and Motorists' Association Limited v Bradley [2002] NSWSC 788, New South Wales Supreme Court, Windeyer J, 28 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc788.html](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc788.html%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Background

Members of the National Roads and Motorists' Association Ltd (NRMA), under section 249N of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) (the Act), proposed that a number of resolutions be put to a general meeting of NRMA members on 17 October 2002. In response, NRMA sought declarations that three of these resolutions be declared to be invalid, so that NRMA would not have to submit them to the general meeting of members. Alternatively, NRMA sought an order under section 1322(4)(d) of the Act extending the time for consideration of these resolutions until the date of the annual general meeting of members, 27 November 2002. Notwithstanding the validity of the proposed resolutions, in the event that this order was made by the court, the resolutions would not have to be put to the members until this date.

Mr David Bradley represented NRMA members who had signed notices under section 249N of the Act in relation to these resolutions.

(2) The resolutions

First, the members sought to put forward as an ordinary resolution:

'That the National Roads and Motorists' Association Limited do all such things as may be necessary in respect of proceedings 4454/01 commenced by the association in the Equity Division of the Supreme Court of New South Wales against John Fairfax Publications Pty Ltd and others:

(a) To release and discharge the following from all undertakings to, and orders (including costs orders) of the Court:

- John Fairfax Publications Pty Ltd
- Anne Lampe
- Kate Askew
- AAP Information Services Pty Ltd
- Belinda Tasker

(b) To cause the proceedings to be discontinued or dismissed.'

Rule 52 of NRMA's constitution provides that subject to the constitution, the management and control of the Association and the business and affairs of the Association are vested in the Directors, who may exercise all powers and do all acts or things that are not expressly required to be exercised or done by the Association in a meeting of members. This rule further states that no rule or resolution passed by a meeting of members shall invalidate prior acts of the Directors where these acts would have been valid if the rule or resolution was not passed.

NRMA submitted that this resolution sought to provide the members with powers which the NRMA constitution vested in the directors, and that for this reason the resolution was invalid. Windeyer J agreed, finding that the resolution was beyond the powers of the members in a general meeting, and as a result, NRMA did not have to put this resolution to their members.

The second resolution was also sought to be put forward as an ordinary resolution:

'That National Roads and Motorists' Association Limited decline to pay, or assist by way of any payment for the legal costs incurred by the Association's former president, Mr N Whitlam, in proceedings 4421/01 commenced by the Australian Securities and Investments Commission against Mr N Whitlam in the Equity Division of the Supreme Court of New South Wales, and any appeal therefrom.'

Section 199A(3)(c) of the Act provides that a company must not indemnify a person against legal costs in defending an action for liability incurred as an officer of the company where the costs are incurred in defending or resisting proceedings brought by ASIC and the grounds for making the order are established to the satisfaction of the Court.

Rule 159 of the NRMA constitution provides that every officer, auditor or agent of the association is to be indemnified by the association against any liability incurred in that capacity, unless precluded by law. Windeyer J noted that this rule operated subject to the Act, which prohibits such payments in certain circumstances.

In the case brought by ASIC against Mr Whitlam, the court had made orders against the defendant, and Windeyer J found that if the appeals from this proceeding failed, then under the Act NRMA could not pay for, or contribute towards Mr Whitlam's costs in these proceedings. Further, Windeyer J considered that Rule 159 prevented this second resolution from being valid, because the rule is binding on all members and any resolution passed contrary to this rule would therefore be invalid.

The third resolution proposed to be moved as a special resolution provided:

'To consider, and if thought fit, pass the following resolution as a special resolution:

1 That the Constitution of the National Roads and Motorists' Association Limited is modified;

(a) by deleting Rule 54 and by substituting in its place the following new Rule: "54. With effect from the conclusion of the General Meeting held on October 2002 the number of Directors shall be reduced to seven";

(b) by deleting from Rule 56 the words and symbols "in 2001 and in 2003, 8" and by
substituting instead the words and symbols "in 2003, 3";

(c) by deleting from Rule 56 the symbol "6" and by substituting the symbol "3";

(d) by deleting from Rule 57 the words "who are to retire from office" and by substituting instead the words "who by count are to cease to hold office";

(e) by deleting from Rule 78 the symbol "6" and by substituting in its place the symbol "3";

(f) by adding to Rule 89 next after the word "services" the words "and special services in Rule 93"; and

(g) by deleting from Rule 93 the words "as Board of Directors may determine" and by substituting instead the words "as the members at a meeting of members may approve".

2 That the modification made in resolution 1 shall take effect forthwith at the conclusion of the General meeting held in October 2002.'

NRMA argued that this resolution was invalid on two grounds, firstly because it was contrary to the provisions of section 203D of the Act, which sets out the procedure for the removal of directors by resolution of the members. Sub-paragraph 1(a) of this resolution would effectively remove seven of the 14 current directors of NRMA from office, with no way of determining which of the directors would remain. As a result, Windeyer J found that it indirectly dealt with the removal of directors, and because it did not comply with the requirements of section 203D of the Act was an invalid resolution.

Alternatively NRMA argued that this resolution was invalid because if it were passed, the provisions of the constitution as changed would be in conflict with the provisions which would remain. In relation to the proposed amendment of Rule 54, Windeyer J agreed, finding that the resolution as drafted would have the effect of reducing the number of directors from 14 to seven without any procedure for determining who would remain in office, and the next election of directors not taking place until 2003. Windeyer J noted that certainty is essential in the management and control of public companies, and if the proposed amendment to Rule 54 was passed there would be no certainty, and more likely chaos. His Honour held that the directors of NRMA should not be required to put the proposed resolution regarding the amendment of this rule to the members.

Sub-paragraphs 1(b), (c), (d) and (e) of the third resolution were considered by the court to be dependent upon the amendment to Rule 54, and so were held to be invalid on this ground. However, the proposed amendments to Rules 89 and 93 were found to relate to the payment of directors, and Windeyer J considered this to be a completely different subject matter from the reduction in the number of directors. As a result, he dismissed the argument that these resolutions were part of a package, and found that sub-paragraphs 1(f) and (g) were in fact valid resolutions.

Having declared the first and second resolutions proposed by the members, along with sub-paragraphs 1(a), (b), (c), (d) and (e) of the third resolution to be invalid, Windeyer J went on to consider whether in relation to sub-paragraphs 1(f) and (g) an order should be made under the Act to extend the time for consideration of these resolutions until 27 November 2002. The court found that it was appropriate to make such an order, noting that Mr Bradley was agreeable to this.

Paragraph 2 of the third resolution was not to be put before the members at the meeting of 17 October 2002, based on the order made in respect of paragraph 1 of this resolution.

In closing, Windeyer J called for legislative reform to prevent this company from being subject to a law where meetings can be called on a notice signed by one hundred members out of a total of around two million members.

(B) COMPANY NOT REQUIRED TO DISTRIBUTE A MEMBERS' STATEMENT TO MEMBERS
(By Sean Tully, Phillips Fox)

NRMA v Snodgrass [2002] NSWSC 811, New South Wales Supreme Court, Campbell J, 30 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc811.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc811.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Background

Mr Snodgrass, on behalf of himself and some 500 other members of the National Roads and Motorists' Association Limited ('NRMA'), successfully requisitioned for the holding of an extraordinary general meeting of NRMA. The meeting is due to be held on 17 October 2002.

Mr Snodgrass wished to have a members' statement included in the documentation to be sent to shareholders of NRMA in relation to the extraordinary general meeting. Section 249P(1)(a) of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) provides that members may request a company to give to all its members a statement provided by the members making a request about a resolution that is proposed to be moved at a general meeting. Section 249P(6) provides that, after receiving the request, the company must distribute to all its members a copy of the statement at the same time, or as soon as practical afterwards, and in the same way, as it gives notice of a general meeting. However, section 249P(9) provides that the company need not comply with the request if the statement is more than 1,000 words long or is defamatory.

(2) The application

NRMA sought declarations that the document supplied to it by Mr Snodgrass was defamatory within the meaning of section 249P(9) of the Corporations Act, and that NRMA was not required to distribute that document to its members.

In considering the meaning of 'defamatory' in section 249P of the Corporations Act, Campbell J accepted the submission made by Mr McHugh, for NRMA, that section 249P(9) should be construed so that the word 'defamatory' is given its usual meaning at common law - namely, whether the meaning of the publication in question has a tendency to lower the plaintiff in the estimate of the ordinary reasonable reader. In other words, Campbell J concluded that in deciding whether a statement is defamatory, one looks only to the meaning of the statement, not the availability of defences.

Campbell J added that 'often in defamation litigation, it is necessary for there to be interlocutory procedures such as discovery or interrogatories to explore the question of whether any defences are available. It would often be very hard for a company, which received a statement from a member, to make a properly informed decision about whether any of these defences were available. That Mr McHugh's construction of section 249P(a) avoids these practical difficulties provides comfort that that construction is the one Parliament intended.'

His Honour stated that 'the fact that debate will, to some extent, be stifled in a situation such as the present is not, in my view, a sufficient reason to alter what appears to be the meaning of the words in their ordinary meaning, particularly when the Court has previously construed a legislative predecessor of section 249P so that 'defamatory' is construed in the way for which Mr McHugh contends'.

Against that background, Campbell J considered the statement itself. In relation to one particular matter, Campbell J was of the view that a reader could draw the conclusion that a person charged with carrying out some functions for NRMA had advanced his own interests in an improper way. His Honour stated that that is the sort of conclusion which would result in the material being defamatory. His Honour was also of the view that the ordinary reader of the material could draw from it, and indeed would be likely to draw from it, a conclusion that particular directors had engaged in a cover-up. His Honour stated that it seemed to him that the statement was defamatory for that reason also.

Mr Snodgrass invoked the desirability of free speech, and submitted that:

- all the facts that were in the statement were correct;
- it was in the public interest for the statements to be published;
- he needed to be able to publish the statements in the interests of proper corporate governance;
- the statement related only to the people who were criticised in their role within NRMA;
- if anyone accepts a job as a director, they must accept with it the prospect that there might be a measure of criticism;
- suspicion has been aroused by the conduct of the directors themselves, and that his statement was merely a statement which pointed out matters which caused such suspicion to be raised.

Campbell J stated that if one were making a decision about what conduct was desirable, completely devoid of any statutory context, the arguments put forward by Mr Snodgrass would undoubtedly have some force. However, His Honour stated that 'it is not for me to say whether in such a context these arguments would ultimately be ones which would prevail. The point for present purposes is that we are not in such a context, free of statutory controls. The decision needs to be made by reference to the obligation which Parliament has imposed on companies under section 249P to distribute statements to members and, equally, upon the qualification contained in Section 249P(9)(a) upon that obligation.'

His Honour therefore declared that:

(a) the statement was defamatory within the meaning of Section 249P(9)(a) of the Corporations Act; and

(b) NRMA was not required to distribute the statement to its members.

(C) APPOINTMENT OF AN INTERIM RECEIVER AND MANAGER TO A CORPORATE TRUSTEE
(By Katie Higgins, Mallesons Stephen Jaques)

Cheung v Makmur Australasia Pty Ltd [2002] VSC 335, Victorian Supreme Court, Habersberger J, 16 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/vic/2002/august/2002vsc335.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2002/august/2002vsc335.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Summary

The Court considered the circumstances in which it will appoint a receiver of a company and/or of trust property. The Court found that the circumstances in this case did not warrant appointment of a receiver of the corporate trustee of the trust property nor of the trust property (specifically, the Court found that the plaintiff's concerns in relation to running the business the subject of the dispute were not as acute as he suggested). Instead, Habersberger J was satisfied that the suggested undertakings by the defendants (which related to operating the business and distributions to shareholders and beneficiaries) were adequate protection.

(2) Facts

Makmur Enterprises Pty Ltd ("MEPL") manufactures and sells Chinese frozen snack food. The company was established by Makmur Tjangdjaja (since deceased). MFAPL provides marketing, promotion and distribution services to MEPL.

MAPL is the trustee of the Investment Trust (the purpose of which is to own property, including the property on which MEPL and MFPAL operate their business) and the Provision Trust (the purpose of which is to distribute profits of MEPL). MAPL holds shares in MEPL, both as trustee for the Investment Trust, and as trustee of the Provision Trust. The beneficiaries of the Investment Trust and the Provision Trust (together "Trusts") are various descendants of Makmur Tjangdjaja.

Other shareholders of MEPL include the plaintiff and one of the defendants (each a descendant of Mr Makmar) and other family members. The plaintiff was also, until recently, a director of MAPL and MEPL (together with other family members).

Over the course of a few months a majority of the respective shareholders of MAPL and MEPL removed the plaintiff as director of MAPL and as managing director of MEPL. The directors of MAPL then purported to pass a resolution vesting the beneficial interests in the Provision Trust.

The plaintiff made an application to the Court for the appointment of an interim receiver and manager of each of MAPL, the Investment Trust and the Provision Trust until the hearing and determination of the proceedings commenced against MEPL for wrongful dismissal. The plaintiff was concerned that MAPL had breached its duties to the Trusts and to the beneficiaries, and that MAPL would not act in the best interests of the Trusts and the beneficiaries in the future.

(3) The law

Regarding appointment of a receiver and manager of a company, section 37(1) of the [Supreme Court Act 1986 No. 110 (Vic)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=248" \t "default) empowers the Court to appoint a receiver when it is "just and convenient" to do so. Section 1323 of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) provides that a Court may, on the application of an "aggrieved person" appoint a receiver and manager of the property of the company, where it considers it necessary or desirable to do so for the purpose of protecting the interests of the aggrieved person to whom the company is liable.

Regarding the appointment of a receiver of trust property, the Court may appoint a receiver of trust property where that step is necessary for the "well-being of the trust" or "the safety of the trust property" (Martyniuk v King [2000] VSC 319). However the case law suggests that this should be exercised with care and caution, since receivership is a "drastic course allowed only under pressing circumstances" (National Australia Bank Limited v Bond Brewing Holdings Limited [1991] 1 VR 529).

(4) The decision

Habersberger J was not convinced that the trust property was in jeopardy, particularly given that the plaintiff's complaint was limited to more general expressions of concern about the successful management of MEPL in his absence (and the available evidence indicated that the business of MEPL had apparently operated satisfactorily since the plaintiff's removal as managing director). Nor was Habersberger J satisfied that the problems with running the businesses were as acute as suggested by the plaintiff. Habersberger J also noted that there was substance in one defendant's submission that the plaintiff was using the application as a possible means of restoring himself to the position of manager of MEPL.

Further, Habersberger J did not consider that, taken by itself, the deadlock between the plaintiff and the third defendant (the two appointors of the Trusts) was sufficient to justify the appointment of a receiver to MAPL.

Habersberger J concluded that that the suggested undertakings on the part of the defendants (by their respective counsel) in relation to the conduct of the business and distribution to shareholders and beneficiaries gave adequate protection, and that it was not necessary to go to the expense of appointing a receiver to the 99.5% shareholder of a solvent and financially successful business.

(D) APPLICATION OF ACCOUNTING STANDARDS IN PROCEEDINGS BEFORE THE COMPANIES AUDITORS AND LIQUIDATORS DISCIPLINARY BOARD
(By Belinda Bradberry, Mallesons Stephen Jaques)

Australian Securities and Investments Commission v Companies Auditors and Liquidators Disciplinary Board [2002] FCA 1066, Federal Court of Australia, New South Wales District Registry, Whitlam J, 28 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/federal/2002/august/2002fca1066.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2002/august/2002fca1066.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Background

In 1997 Holyman Limited ("Holyman") purchased all of the issued share capital in Union Shipping Group Limited ("USGL") from Brierley Investments Limited ("Brierley"). The sale agreement was executed on 20 June 1997 and the sale was completed on 3 September 1997. Holyman obtained bridging finance to pay the purchase price for the shares. On 10 September Holyman issued converting preference shares, using the moneys raised to repay the bridging finance.

Holyman included in its accounts for the half-year ended 30 June 1997 the whole of USGL's profit for the half year on the basis that Holyman obtained control of and acquired the shares in USGL on 1 January 1997, despite the fact that the sale agreement was not executed until June of that year. There was a material difference between the profit recorded in Holyman's accounts and the loss that would have resulted if 20 June 1997 had been used as the operative date, as this would only enable Holyman to recognise that portion of the USGL profit earned from 20 June onwards.

In its balance sheet, Holyman recognised, as part of its share capital and reserves, the par value of the converting preference shares and the net premium realised on those shares. However, the shares were not issued by Holyman until 10 September 1997. Additionally, the loan in respect of the purchase price payable for the USGL shares was understated significantly in the balance sheet.

Mr Gulson was hired to audit the consolidated accounts of Holyman for the half-year ended 30 June 1997. Upon completing the audit, Gulson signed an unqualified audit report.

(2) Companies Auditors and Liquidators Disciplinary Board

ASIC made an application to the Companies Auditors and Liquidators Disciplinary Board ("Board") for an order that Gulson's registration as an auditor be cancelled or suspended under section 1292(1)(d) of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default), on the basis that Gulson had failed to carry out or perform adequately the duties of a registered auditor in his review of Holyman's consolidated accounts. ASIC raised two contentions for consideration by the Board.

ASIC's first contention was that Gulson should have formed the belief that the accounts did not comply with AASB1024: Consolidated Accounts, because Holyman's calculation of profits was based on the assumption that the USGL shares were acquired on 1 January 1997 when in fact it was not reasonable to conclude that Holyman had either obtained control of USGL or acquired the shares any earlier than 20 June 1997.

Secondly, ASIC contended that Gulson ought to have formed the belief that the accounts did not comply with AASB1002: Events Occurring After Balance Date, because Holyman had included in its accounts the value of the shares even though they were yet to be issued at the date of the accounts, and also because the loan to Holyman to purchase the USGL shares had been significantly understated in the accounts.

The Board rejected ASIC's first contention and instead found that the date of the acquisition of the USGL shares was not relevant to Gulson's review of the accounts. It took the view that the date on which Holyman, as parent company, took control of USGL, being the subsidiary, was the relevant date. The Board was not satisfied that Gulson failed, when considering the "control date", to carry out his review in accordance with Auditing Standard AUS 902: Review of Financial Reports, and with AASB1024.

The Board accepted the second contention, finding that Holyman's treatment of the liability and the share issue should have caused Gulson to question the accounts and to qualify his report. Consequently, the Board severely reprimanded Gulson and required him to attend advanced level courses on accounting standards.

(3) Federal Court

Both ASIC and Gulson brought applications in the Federal Court seeking an order for review of the Board's decision, under the [Administrative Decisions (Judicial Review) Act 1977 No. 59 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=7119" \t "default).

(a) ASIC's first contention: Inclusion of USGL profits

ASIC submitted that the Board misconstrued AASB1024 by applying the criteria of control instead of acquisition when determining whether the whole of USGL's profit could be recognised in Holyman's accounts. Whitlam J accepted this submission. He noted that whilst the adoption in AASB1024 of control as the criterion for determining a parent/subsidiary relationship enabled identification of the economic entity for which consolidated accounts must be prepared, the extent of the parent company's ownership interest remains important. Paragraph 34 of AASB1024 requires disclosure of any portion of the operating profit attributable to "outside equity interests". Whitlam J went on to point out that it is clear from the Standard that consolidation adjustments are to be made to reflect acquisitions of ownership interests by the parent entity. His Honour found that the Board's misconstruction of the accounting standard involved an error of law, and therefore its decision must be set aside. The contention was referred back to the Board for further consideration according to law.

(b) ASIC's second contention: Recognition of value of shares and understatement of loan

Gulson challenged the Board's finding on the second contention on two grounds. Firstly, Gulson argued that the Board erred in finding that ASIC had discharged the required standard of proof when considering whether he had properly applied AASB1002. However, Whitlam J found that the Board applied a "high standard of proof" in view of the seriousness of the contentions and the possible impact on Gulson, and that it was properly satisfied that ASIC had discharged the requisite standard. Secondly, Gulson disputed the correctness of the Board's finding that his failure to apply AASB1002 was material. However, His Honour found that the assessment of materiality is a matter of judgment for the Board. In any case, His Honour was in agreement with the Board that the particular items and amounts in question were material.

Finally Gulson challenged the Board's conclusion that section 1292(1)(d) of the Corporations Act was satisfied as a direct consequence of its finding that he had not properly applied AASB1002. However, His Honour found that the Board did not simply conclude that Gulson should have qualified his report. The Board had also concluded that Gulson's failure to qualify his report satisfied the Board that he had failed to adequately and properly perform the duties of an auditor, thereby establishing the grounds set out in section 1292(1)(d). Gulson's application was dismissed.

(4) Conclusion

When considering section 1292(1)(d) of the Corporations Act:

(a) it is appropriate for the Board to examine and interpret relevant accounting and auditing standards and make an assessment as to whether the auditor has complied with those standards in signing off on a company's accounts; and

(b) evidence of an auditor's failure to comply with the relevant standards will prima facie be sufficient grounds for a finding by the Board that the auditor has failed to properly or adequately carry out his or her duties as an auditor.

(E) APPLICATION TO WIND UP MANAGED INVESTMENT SCHEME
(Bart Price, Blake Dawson Waldron)

Australian Securities and Investments Commission v McNamara [2002] FCA 1005, Federal Court of Australia, Mansfield J, 19 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/federal/2002/august/2002fca1005.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2002/august/2002fca1005.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Introduction

ASIC sought orders to wind up a managed investment scheme on the basis that individuals were carrying on a securities business or financial services business without holding the appropriate licenses and had issued financial products without providing an appropriate product disclosure statement.

Joseph McNamara ("McNamara") and Bernold Glaser ("Glaser") established the Archipelago Finance Ltd Partnership ("Archipelago Finance") to provide finance to the Archipelago Site Survey Foundation Inc ("ASSF"). ASSF had entered into a joint venture to carry out the survey and recovery of shipwrecks with Adelaide Australian Investment Service Pty Ltd ("AAIS"). AAIS was responsible for the management of Archipelago Finance.

McNamara and Gary Johnstone ("Johnstone") sought to raise funds for Archipelago Finance, raising over $300,000 from more than 55 investors.

ASIC argued that there had been a contravention of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) ("Corporations Act") in that:

(a) the defendants had sought to carry on a securities business without holding a dealers license or being exempt from holding a dealers license, contrary to section 780(1) of the Corporations Act;

(b) the defendants had carried on a financial services business without holding an Australian financial services license, contrary to section 911A(1) of the Corporations Act; and

(c) the defendants had issued financial products without a product disclosure statement contrary to section 1012B(3) of the Corporations Act.

On this basis ASIC applied for orders to wind up the scheme of Archipelago Finance that investors had invested in.

(2) "Carrying on a Securities Business" - section 780(1) of the Corporations Act

When examining if the defendants had carried on a securities business, the court focused on whether the issuing of units was a managed investment scheme.

An individual will be carrying on a securities business if they make or attempt to make or induce or attempt to induce an agreement with a person to acquire or dispose of securities in accordance with sections 9 and 93 of the Corporations Act.

The term "securities" is defined in the Corporations Act to include interests in a managed investment scheme, referred to in section 92(2) of the Corporations Act.

Section 9 provides that a "managed investment scheme" has the following features:

- people contribute money as consideration to acquire rights to benefits of the scheme;
- any of the contributions are to be pooled, or used in a common enterprise to produce financial benefits to members who hold interests in the scheme; and
- the members do not have day to day control over the operation of the scheme.

Justice Mansfield found that Archipelago Finance was a managed investment scheme as there was a scheme whereby individuals purchased units in Archipelago Finance which were used to finance marine salvage operations by ASSF, with a view to obtaining a financial return.

The court held that the conduct of AAIS, McNamara and Johnstone in obtaining investors in Archipelago Finance was an offer and acquisition of interests in a managed investment scheme. Justice Mansfield found that AAIS, McNamara and Johnstone had sought to carry on the business of selling units which was systematic, repetitious and continuous. None of the entities had a dealers license, breaching the Act.

(3) "Carrying on a Securities Business" - section 991A(1) of the Corporations Act

The court examined whether Archipelago Finance, McNamara and Johnstone had carried out a financial services business without an Australian financial services license.

A business of providing financial services refers to dealing in a financial product which includes issuing units in an unregistered managed investment scheme pursuant to sections 764A(1), 766A(1) and 766C(1) of the Corporations Act.

The court found that Archipelago Finance was the issuer of a financial product by providing units in a systematic, repetitious and continuous manner and as a result required an Australian Financial Services license.

In addition, McNamara and Johnstone had arranged for investors to apply for and acquire units in Archipelago Finance and did so without an Australian Financial Services license.

The court held Archipelago Finance, McNamara and Johnstone all breached sections 991A(1) and 601ED of the Corporations Act.

(4) "Product Disclosure Statement" - section 1012B of the Corporations Act

An issuer of a financial product must give a person a Product Disclosure Statement with the issue of a financial product pursuant to sections 1011B and 1012B(3) of the Corporations Act.

Archipelago Finance was required to give a Product Disclosure Statement to each individual to whom an offer was made to issue units in the managed investment scheme.

The court looked at whether a statement given to investors constituted a Product Disclosure Statement. The court held the statement given to shareholders was not a Product Disclosure Statement because:

- it did not properly display the words "Product Disclosure Statement" required by section 1013B of the Corporations Act;
- it did not include enough information, such as the information which might reasonably be expected to have a material influence on the decision of a reasonable person whether to acquire units in Archipelago Finance contravening section 1013C and 1013E of the Corporations Act; and
- the statement was not adequately dated contravening section 1013G of the Corporations Act

(5) "Application to Wind Up The Scheme" - section 601EE of the Corporations Act

ASIC applied to the court to wind up the managed investment scheme pursuant to section 601EE of the Corporations Act, on the basis that a person had operated a managed investment scheme in contravention of section 601ED of the Corporations Act,

The court considered whether it was just and equitable to wind up the scheme in accordance with section 461(1)(k) of the Corporations Act.

The court held that it was in the public interest that the scheme be wound up on the basis that those individuals issued units in Archipelago Finance would be better protected if the scheme was wound up by the appointment of a liquidator.

(6) Conclusion

The court will ensure that when individuals have invested in a managed investment scheme, all legal requirements to protect investors are complied with, so that each individual investor is protected. If that has not occurred, ASIC will seek to protect investors and this may include an application to wind up the scheme.

(F) THE RELEVANCE OF CHAPTER 6 PRINCIPLES TO SCHEMES OF ARRANGEMENT
(Fatmir Badali, Blake Dawson Waldron)

Re Ranger Minerals Ltd; ex parte Ranger Minerals Ltd [2002] WASC 207, Supreme Court of Western Australia 207, Parker J, 16 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/wa/2002/august/2002wasc0207.htm](http://cclsr.law.unimelb.edu.au/judgments/states/wa/2002/august/2002wasc0207.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

Re Ranger Minerals Ltd was an application pursuant to section 411(1) of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) seeking a court order of a meeting of Ranger shareholders to consider a scheme of arrangement (the "Scheme") to restructure Ranger Minerals Ltd ("Ranger"), whereby Ranger will become a wholly owned subsidiary of Perilya Ltd ("Perilya"). The Australian Securities and Investments Commission ("ASIC") objected to the Scheme on the basis that the value of the Scheme was significantly below the consideration that Perilya agreed to pay a potential takeover rival for its Ranger shares (Revesco Group Limited ("Revesco")), and thus offended the equality principle under section 602(c).

Ranger was able to satisfy the Court that the Scheme was not propounded for the purpose of avoiding any part of Chapter 6 of the Corporations Act. ASIC's approach to the value of the consideration in takeovers had no compelling relevance in determining this case on its facts.

(1) The facts

Under the Scheme, it was proposed that all Ranger shares will be transferred to Perilya, in consideration for which Perilya will issue 3 Perilya shares for every 4 Ranger shares received. If the scheme is implemented, Ranger shareholders will also get a fully franked cash dividend of 5.5 cents per share and Ranger will be de-listed from the Australian Stock Exchange.

On 18 April 2002, Revesco announced an off-market takeover bid for shares in Ranger. On 15 May 2002, by a Substantial Shareholders Notice, Revesco announced acceptances under its offer for 7.56% of Ranger. On 20 May 2002 Ranger issued a Target's Statement responding to Revesco's Bidder's Statement recommending Ranger shareholders reject Revesco's offer. An independent expert's report included in the Target Statement concluded that the Revesco bid was neither fair nor reasonable to Ranger's shareholders.

At the time of time of the announcement of the Revesco bid, Revesco and Ranger had a common Chairman. The Chairman resigned in April, though remained a director until 6 July 2002. Ranger's directors (excluding the Chairman (due to conflicts of interest)) held the view that Revesco's bid offered inadequate value to Ranger's shareholders.

In the week preceding 27 May 2002, Perilya and Ranger discussed the possibility of a merger. Perilya proposed a merger by way of a scheme of arrangement. On 27 May 2002, Perilya and Ranger agreed to a merger by way of scheme of arrangement and concluded a Merger Implementation Agreement that day. Extensive detailed evidence was placed before the Court disclosing sound commercial reasons why each company agreed to the Scheme and preferred a Chapter 5 scheme to a Chapter 6 takeover.

On 5 and 17 June 2002, Revesco increased its bid for Ranger. On 3 July 2002, a representative of Revesco approached a Perilya director to discuss the acquisition by Perilya of Revesco's Ranger Shares. Negotiations culminated in a put and call option agreement between Revesco and Perilya over Ranger shares (the "Revesco Agreement"), with Ranger's full knowledge and support.

Under the Revesco Agreement, Revesco granted a call option and Perilya a put option over Ranger shares owned by Revesco at an exercise price of $0.63 per share, together with a "resolution fee" of $1.5 million in consideration of Revesco effectively agreeing not to extend its bid.

Payment of the resolution fee was subject to a clawback as the total number of shares concerned was uncertain due to orders by the Takeover Panel requiring the cancellation of certain acceptances under the Revesco bid. Sufficient cancelled acceptances were reaccepted to allow the full resolution fee to be paid to Revesco. On 22 July 2002 Revesco announced that the takeover bid for Ranger had closed with Revesco receiving acceptances for 19.28% of Ranger's issued share capital. Perilya will not vote these shares should a shareholders' meeting be ordered. Revesco also agreed with Perilya that Revesco will not vote any shares it may hold which are the subject of a put and call agreement. Parker J noted that if the resolution fee was included in the calculation price per Ranger share paid or agreed to be paid by Perilya to Revesco, the price was approximately $0.759.

(2) ASIC opposition

ASIC did not produce to the Court a written statement that it had no objection to the scheme in accordance with section 411(17)(b). The Court therefore had to be satisfied that "the compromise or arrangement had not been proposed for the purpose of enabling any person to avoid the operation of any of the provisions of Chapter 6", before approving the Scheme. The proponents of a scheme have the burden of establishing this.

ASIC appeared at the hearing to oppose Ranger's application. ASIC contended that the value of the scheme was significantly below the consideration that Perilya agreed to pay Revesco for its Ranger shares under the Revesco agreement (ie $0.759 per Ranger share). ASIC submitted that the consideration paid to Revesco was greater than the market value of the scheme consideration from the date of the announcement of the merger. ASIC further submitted that even if the resolution fee was not taken into account, the consideration agreed with Revesco of $0.63 per Ranger share had been greater than the market value of the scheme consideration since about 12 July 2002.

In assessing the scheme, ASIC submitted that the provisions of Chapter 6 are of assistance (ie the scheme may be viewed as analogous to a takeover by Perilya of Ranger). Accordingly, ASIC contended that the scheme offended the equality principle under section 602(c). ASIC relied on section 621(3) (minimum bid price principle) and section 623 (collateral benefits prohibition) in support of this contention.

Such an approach led ASIC to submit that an order for the convening of a meeting under section 411(1) should only be made if the value of consideration under the Scheme matches, as far as practicable, the consideration paid under the Revesco Agreement. ASIC suggested the consideration be determined according to the averaged market price for a number of trading days up to the date of the hearing, or the date when the explanatory statement was dispatched, or by use of a formula based upon the trading price of Perilya shares from the date of the hearing to the date on which consideration is given to Ranger shareholders.

Ranger responded by arguing there to be no direct application of Chapter 6 requirements to a Part 5.1 scheme, and that it would be inappropriate, if not impossible, to apply Chapter 6 requirements to the Scheme. Neither statute, nor ASIC policy required that consideration must, or should be, measured by reference to market value only. Furthermore, Ranger relied on an independent expert report which valued the Scheme at between $0.80 and $1.26 per Ranger share, as compared with $0.759 under the Revesco Agreement (including the resolution fee). ASIC did not seek to contradict the report, which was brought into existence before the Revesco Agreement was even contemplated.

(3) Improper purpose - avoidance of Chapter 6

Undisputed evidence before the Court found that in March 2002, Perilya committed itself to the acquisition of Ranger's Broken Hill mine, involving an initial outlay of $60 million. At the time of its acquisition it was foreseen by Perilya's directors that Perilya required additional capital in the order of $25 million. It proposed to raise this by way of a share issue. Discussions with stockbrokers were at an advanced stage by the time discussions were held with Ranger. Ranger had cash and liquid reserves in the order of $30 million. If Ranger was to become a wholly owned subsidiary of Perilya, those assets would become available to Perilya and therefore eliminate the need to raise external capital. Without a 100% merger, Perilya would not have unrestricted access to Ranger's cash reserves. For this reason, Perilya wished the proposed merger to be undertaken by way of a scheme of arrangement.

Similarly, Ranger favoured merger with Perilya by way of a scheme of arrangement. Full merger would allow Ranger's cash resources to be readily used to develop the merged asset base, as well as provide capital gains tax rollover protection, amongst other benefits, for its shareholders.

On the evidence, the Court found there to be sound reasons for each company to prefer a merger by way of a scheme of arrangement. As the evidence only showed the Revesco agreement was not in contemplation at the time of the merger on 28 May 2002, it could not have been a purpose of the Scheme to avoid any Chapter 6 implications of the Revesco Agreement. For the purposes of section 411(17)(a) it was only necessary that the Scheme had not been proposed for the purpose of enabling avoidance of any of the provisions of Chapter 6. In this regard the Court considered the purpose, rather than the effect of the Scheme in deciding whether the scheme had been proposed for the purpose of enabling avoidance of any of the provisions of Chapter 6.

(4) The equality principle

ASIC submitted the equality principle espoused under section 602(c) had been offended as the Revesco agreement represented a higher consideration than the scheme consideration, when assessed by reference to the current market price of Perilya shares. ASIC pointed to section 621(3) (which requires the consideration offered for securities in a takeover bid to equal or exceed the maximum consideration the bidder agreed to provide under any agreement during the four months before the date of the bid) and section 623 (which forbids collateral benefits where the benefit: (a) is likely to induce a person (Revesco) to dispose of securities; and (b) where the benefit is not offered to all holders of securities in a bid class under the bid). These provisions apply only to takeovers pursuant to Chapter 6, not to schemes of arrangement the subject of Chapter 5.

The Court felt there may be reason to consider the protections afforded to individual shareholders by Chapter 6 and, where appropriate adopt analogous safeguards to those applicable to conventional takeovers, albeit with necessary adaptations: Re Archean Gold NL (1997) ACSR 143 at 147 per Santow J. This would give practical effect to views expressed by Kirby P in Catto v Ampol (1989) 15 ACLR 307 at 310, that the scheme and takeover provisions should be interpreted, as far as language and apparent purposes permit, in a way "which affords a harmonious, practical and mutually supportive operation to each". Catto v Ampol was a capital reduction case in a statutory context where the equivalents of Chapters 5 and 6 were in separate legislative enactments.

Nevertheless, the Court found material distinctions existed between a takeover and a scheme for a merger. The legislative purposes and policy considerations differ in a number of aspects. The legislature did not apply Chapter 6 provisions to schemes of arrangement. Parker J states (at paragraph 36): "[N]o search to find a harmonious, practical and mutually supportive operation would appear justified if its effective consequence was to apply Chapter 6 in every case as though it was a part of Chapter 5 ... In my view, the extent to which principles and legislative policies reflected in Chapter 6 may usefully have relevance to, and may properly be allowed to weigh in the exercise of discretion when a scheme of arrangement is being considered will be very dependent upon the particular circumstances of the case". Accordingly, the question for the Court was whether there was reason in the exercise of its discretion to seek to ensure that the scheme consideration is fair and would not affect the equality principle of Chapter 6, having regard only to the market value of the consideration.

The Court found neither Chapter 5 nor Chapter 6 required any particular approach be taken to the valuing of an offer (whether takeover or scheme). ASIC policy provided that in valuing quoted securities the bidder should value the share consideration by adopting a volume weighted average market price in the ordinary course of trade two full trading days before the valuation time (at any time of the bidder's choosing up to 5 days before the date of the takeover bid).

The Court found that in the takeover context there were clear justifications for ASIC's policy preference. However, a scheme of arrangement is different in form and elements. The decision whether the scheme will proceed is determined by Court decision and lodgement of the order - a process which ensures shareholders have full and frank disclosure of all relevant issues. In a case such as this, the Court can ensure that facts relating to the acquisition are fully and frankly presented to the shareholders, and that shareholders are assisted by independent expert opinion as to the value of the scheme consideration.

(5) Conclusion

Ranger was able to satisfy the Court, on the evidence, that the scheme was not propounded for the purpose of avoiding any part of Chapter 6. ASIC's approach to the value of the consideration in takeovers had no compelling relevance in determining this case on its facts. It should be noted that the Court was careful to ensure that each scheme of arrangement would be dealt with on a case by case basis, and that application of Chapter 6 principles may be appropriate in other schemes, or even in the approval hearing in the present case.

(G) IS A PREMIUM PAYABLE TO CREDITORS UNDER A DEED OF COMPANY ARRANGEMENT PERMISSIBLE?
(By Cheryl Sullivan, Clayton Utz)

Young (as representative for the Australian Partnership known as Accenture) v Sherman [2002] NSWCA 281, New South Wales Court of Appeal, 28 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswca281.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswca281.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

This decision deals with whether a Deed of Company Arrangement which contains a premium payable to some but not all creditors is contrary to the policy of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) (the "Act") and therefore should be terminated under section 445D(1) of the Act because effect could not be given to it without injustice or undue delay or because the deed or the provision of it relating to the premium was oppressive or unfairly prejudicial to or unfairly discriminatory against Accenture as a creditor.

(1) Background

The deed provided that a 10% "premium" would be paid to creditors if proposed litigation against Accenture was successful and the damages awarded exceeded the admitted claims by at least 10%. If litigation funding could not be sourced within 6 months of execution of the deed, then the company would be placed into liquidation.

At the second meeting of creditors, the majority in number of creditors voted to accept the proposed deed. Accenture, the company's largest creditor in value, voted against the motion. The administrator used his casting vote in favour of the resolution on the basis that he was voting consistently with the majority in number of the creditors (10 to 1, with 1 abstaining) and in line with the recommendations made by him in the report to creditors. The administrator was also mindful of the vested interests of Accenture as the proposed target of the litigation.

The two main issues were whether the administrator was entitled to exercise his casting vote on the motions and whether the deed should be set aside because of the proposed "premium".

(2) Decision

The NSW Court of Appeal found in favour of Accenture and ordered that the orders of the trial judge be set aside and the proceedings be dismissed or, in lieu, that the Deed of Company Arrangement be terminated pursuant to section 445D of the Act.

As to whether the administrator was entitled to exercise his casting vote on the motions, Sheller JA, with whom Hodgson JA and Davies AJA concurred, held that Regulation 5.6.21 of the [Corporations Regulations 2001 No. 193 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56758" \t "default) does not indicate the circumstances in which the person presiding should exercise a casting vote. In considering whether the person presiding exercised the casting vote properly, the correct approach is to weigh up all relevant factors, such as whether any particular class of creditors will be unfairly prejudiced by the proposal, whether the meeting had been given all relevant information and whether the directors stood to gain an unfair advantage. There is no general rule that the administrator should exercise the casting vote to prefer the view of the majority in value over the view of the numerical majority.

Sheller JA held that the "premium" was a gratuity to which none of the creditors would otherwise be entitled in law whether or not the company was wound up and that "it is indefensible in such a context to offer a gratuity to some creditors, albeit the majority numerically, to be paid if the deed is entered into and the litigation is successful". His Honour believed that this would open up a "fertile field for abuse" and therefore was against the policy of the Act and against public interest.

His Honour distinguished the position where a creditor votes in a particular way because the creditor expects to receive a greater dividend.

Hodgson JA added that there was nothing improper in shareholders offering compensation to creditors for a delay in payment even where the creditors would not otherwise be entitled to interest, so long as this is done openly, and is either consented to by all creditors or at least does not affect creditors unequally. In this case, the premium did affect creditors unequally, had no substantive justification and operated as an inducement to some creditors to agree to a result favourable to the directors and unfavourable to another creditor. It was therefore held to be an improper inducement which justified the termination of the deed.

Hodgson JA also considered whether the administrator was required to disclose to the creditors the legal advice received by him as to the prospects of success of the contemplated litigation. It was held that the administrator was required to either disclose the factual circumstances and legal propositions said to give rise to a reasonable cause of action or disclose the legal advice subject to confidentiality undertakings being given to preserve privilege. It was suggested that merely disclosing the fact that legal advice existed which asserted that there were good grounds for legal proceedings, may not be sufficient to enable a creditor facing a disadvantageous vote to make an informed submission as to the merits of the proposal. Also, if the administrator has prospects of litigation funding to finance proceedings against one creditor, the likely terms of that funding should be disclosed if known.

Davies AJA added that whilst the Courts should be reluctant to interfere unless elements of unfairness and inequality are shown, the deed was discriminatory against and oppressive to a creditor. Accenture received no significant benefit from it and any significant moneys to be recovered were to come from them. His Honour viewed the premium as a "bribe" to creditors to vote in favour of the scheme which, if adopted, would preclude examination of the directors for insolvent trading and like matters. Having no commercial rationale, the 10% inducement did not fall within that category of cases where it was proper for the creditors to agree on something other than equality of treatment.

A liquidation would have given greater scope for the achievement of the object of Part 5.3A, namely that the interests of the creditors be maximised, as under the deed the only proceedings taken would be proceedings against Accenture.

Davies AJA also held that as the scheme lacked the inherent character of fairness and equality, the administrator ought not have exercised his casting vote in favour of it.

(3) Comment

The rationale behind this case is the purpose of Part 5.3A, namely to allow the affairs of the company to be administered in a way that "if not possible for the company or its business to continue in existence - results in a better return for the company's creditors and members that would result from an immediate winding up of the company" [section 435A(b)].

In this case, if a cause of action existed against Accenture, a liquidator could have pursued such a right resulting in the creditors receiving a full payment of their debts. The liquidator also would have been able to investigate the directors for insolvent trading and other similar matters which the deed precluded.

Overlying this is the concept of fairness and equality to all creditors. This case is in line with the views taken in Khoury v Zambeena Pty Ltd [1999] NSWCA 402 and Lam Soon Australia Pty Ltd v Molit (No 55) Pty Ltd, (1996) 14 ACLC 1737, and makes it clear that where one creditor or group of creditors suffers a disadvantage, the deed should not be any less beneficial to all creditors than a liquidation.

It is possible that if the deed simply provided for action to be taken against Accenture without the provision of the 10% "premium", then it may not have been seen to be unfairly prejudicial against one of the creditors. What the Court was so strongly against was the possibility of a "bribe", which would have subverted the purpose of Part 5.3A and would clearly have been against public policy.

(H) OBTAINING A COURT ORDER TO VALIDATE AN INVALID COMPANY RESOLUTION
(By Jonathan Joseph, Clayton Utz)

Re Continental Pacific Insurance Co (Aust) Ltd [2002] NSWSC 789, New South Wales Supreme Court, Barrett J, 26 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc789.html](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc789.html%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Issue

This decision deals with the question of whether a resolution made by the board of a public company in contravention of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) ('Act') and the company's constitution can be validated by a court order under section 1322(4)(a) of the Act.

(2) The facts

Section 201A(2) of the Act requires that a public company have at least three directors. Continental Pacific Insurance Co (Aust) Ltd's constitution set a quorum of two for directors' meetings. Despite this, the company had only one director. That director purported to pass a resolution under section 436A to appoint a voluntary administrator. The lack of other directors and quorum meant that the resolution contravened both the Act and the company's constitution.

The administrator subsequently became the liquidator of each company. In an attempt to validate his appointment, he applied to the Court for an order under section 1322(4)(a) validating the resolution.

(3) The law

Section 1322(4)(a) of the Act provides that the Court "may, on application by any interested person, make ... (a) an order declaring that any act, matter or thing purporting to have been done ... under this Act or in relation to a corporation is not invalid by reason of any contravention of a provision of this Act or a provision of the constitution of a corporation". However, section 1322(4)(a) may only be invoked if the pre-requisites in section 1322(6) are satisfied. Section 1322(6) provides that "the Court must not make an order under this section unless it is satisfied:

(a) in the case of an order referred to in paragraph (4)(a):

(i) that the act, matter or thing, or the proceeding, referred to in that paragraph is essentially of a procedural nature;

(ii) that the person or persons concerned in or party to the contravention or failure acted honestly; or

(iii) that it is just and equitable that the order be made; and
...
(c) that no substantial injustice has been or is likely to be caused to any person."

Consequently, the liquidator's claim for an order under section 1322(4)(a) could only be granted if the Court was satisfied as to one of the three matters in sub-sections 1322(6)(a)(i)-(iii), plus the overriding requirement in section 1322(6)(c) that no substantial injustice had been or was likely to be caused to any person.

(4) Decision

Barrett J granted the order sought by the liquidator under section 1322(4)(a). His Honour was satisfied that the sole director had acted honestly (thus satisfying section 1322(6)(a)(ii)) and that, for the reasons outlined below, it was just and equitable that the order sought be made (thus satisfying section 1322(6)(a)(iii)). (Given the satisfaction of two of the pre-requisites in section 1322(6)(a), it was of no consequence that his Honour considered that the absence of the statutory minimum number of directors was not of a procedural nature - and that, therefore, section 1322(6)(a)(i) was not satisfied.) In relation to section 1322(6)(c), his Honour concluded that, for the same reasons, granting an order under section 1322(4)(a) would not cause any substantial injustice to any person.

In reaching his decision, his Honour stressed the importance of the fact that the company was, "at both shareholder and director level, under the sole control and direction of [one person] and that his was the only human mind and will at work within" the company.

In other words, unlike the typical lack of quorum cases, it was not the situation in this instance that there were other directors who could have attended a meeting to consider the resolutions. Nor had the resolution been passed in proceedings that took place in the absence of directors whose participation might have had some bearing on the outcome.

Consequently, his Honour reasoned that "[t]he purported passing of the section 436A resolution and the opinion reflected by that supposed resolution were thus expressions of the opinion and intention of the only person whose decisions were in any way meaningful in relation to the conduct of the affairs of [the] company."

Also relevant to Barrett J's decision was that the company had only one creditor which, it appeared, was content to see the company go into administration.

(5) Comment

The effect of the granting of the order sought by the liquidator was that the initial appointment of the administrator was valid, notwithstanding that it was made in contravention of the Act and the company's constitution.

It will be interesting to observe the extent to which the Courts use their discretion to invoke this section in the future for the purpose of validating resolutions passed by companies in breach of other sections of the Act and/or their constitution. Although Barrett J does not refer to it, the legislative policy behind section 588H(6) must have been a factor in the director's decision to appoint an administrator and, possibly, in his Honour's reasoning as well. Although directors are personally liable for insolvent trading debts, section 588H(6) provides a defence to a director who took reasonable steps to appoint an administrator. A director of an insolvent and inquorate company would obviously have difficulties in recruiting new members to the company's board, so this decision provides a practical solution to that problem. At the same time, of course, the fact that the Court's order is related to the legislative policy of section 588H(6) may limit the wider application of this precedent.

(I) BANNING ORDERS AND PECUNIARY PENALTIES FOR RELATED PARTY PAYMENTS UNDER THE CORPORATIONS LAW
(Luke Westmore, Freehills)

Australian Securities and Investments Commission v William Arthur Forge [2002] NSWSC 760, New South Wales Supreme Court, Foster AJ, 28 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc760.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2002/august/2002nswsc760.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Background

The Australian Securities and Investments Commission (ASIC) sought various declarations and orders against the defendants in respect of conduct occurring in 1998, which was alleged to have been in breach of certain provisions of the Corporations Law (the Law) then in force. ASIC sought civil penalty orders against each defendant being declarations under section 1317EA(3) and orders under section 1317EA(3) of the Law. Furthermore, ASIC alleged that the conduct engaged in by each of the defendants involved contraventions of provisions of the Law that were in place in 1998, being sections 232(2), 232(4), 232(6), 243ZE(2) and 243ZE(3).

(2) The facts

The first defendant, Mr Forge, was the sole director and secretary of the sixth defendant, Bisoya Pty Ltd (Bisoya). The second defendant, Mr Endrez, and the third defendant, Mrs Endrez, were husband and wife. The fourth defendant, Allan Endrez was their son. The fifth defendant, Kamanga Holdings Pty Limited (Kamanga) is a family company of the Endrez family.

Mr and Mrs Endrez and Allan Endrez were at different times directors of the Company CTC Resources NL (CTC). In April 1991 Mrs Endrez was appointed a director of CTC. On 11 June 1993 Allan Endrez resigned as director and secretary and Mr Endrez was appointed secretary in his place. Mr Forge was appointed a director of CTC on 9 September 1994.

The proceedings were bought about as a result of events that occurred in April 1998. In that month CTC received $6,000,000 from the Commonwealth of Australia. This was characterised as payment for 60,000 redeemable convertible non- cumulative A- Class preference shares with a issue price of $10 per share.

After a portion of the amount received was invested in a Commercial facility, the remaining $3,596,348.90 was disbursed at various times in 1998. Eight transactions were alleged to have breached the Law. These transactions were made up of 5 payments to Kamanga from CTC which were approved by Mr Endrez, Mrs Endrez, Allan Endrez and Mr Forge as officers of CTC, the most significant of which was a payment for $2,205,000, and 3 payments aggregating to over $345,000 to Bisoya from CTC approved by Mr Endrez, Mrs Endrez and Allan Endrez as officers of CTC. These payments were said to represent management fees.

The auditors of the Company had raised questions in relation to these payments, citing in a report that, given the poor performance of CTC, it was difficult to maintain an argument that the remuneration was reasonable. Further information was requested from the company and was not given. The auditors reached the view that the transactions were not commercial or in compliance with the Law. On February 1 2000, the auditors wrote to ASIC indicating that until the directors had furnished them with a full set of financial statements they would be unable to finalise the audit for the year ended 30 June 1998.

(3) The role of Allan Endrez

Allan Endrez attempted to argue that at no relevant time was he concerned in the management of the company or involved in the eight transactions. ASIC argued that during the period of the relevant transactions, he was an officer of CTC. Section 232(1) of the Law provided that the term officer, in relation to a corporation, means a director, secretary or executive officer of the corporation. An executive officer is a person who is concerned in, or takes part in, the management of the body (regardless of the person's designation and whether or not the person is a director of the body). Although Allan Endrez attempted to define his role as a "corporate adviser", Foster AJ found that following being disqualified from being able to act as a director in 1993, the role of corporate adviser he adopted was in truth "...no more than an artifice to avoid the consequences of disqualification".

(4) Were Kamanga and Bisoya related parties of CTC?

The defendants denied that Kamanga was a related party within the meaning of s243F of the Law. It was established that Mr Endrez had been a director of Kamanga since 1987 and owned 40% of its shares, and that Allan Endrez owned the remaining 60% of the shares. As a result Kamanga was a related party of CTC.

Similarly, the ownership of Bisoya was divided equally between the first defendant, who was at the relevant times a director of CTC, and his wife. The combined effect of sections 243F(1)(a)(d) and (f) was to make Bisoya a related party at the relevant time.

(5) Did Kamanga and Bisoya receive financial benefits pursuant to s 243G of the Corporations Law?

Foster AJ reached the conclusion that all of the eight transactions constituted a financial benefit.

(6) The contraventions

Foster AJ explored what had been said judicially about the sections that were breached. As to the duty to act honestly required by section 232(2) of the Law, Australian Growth Resources Corp Pty Ltd v Van Reesema (1988) 13 ACLR 261 was relied upon. In that case, King CJ stated that the section embodied a concept analogous to constructive fraud in that the dishonesty involved does not involve moral turpitude.

In relation to section 232(6), Foster AJ relied on the principle espoused by the High Court in R v Byrnes (1995) 183 CLR 501, where it was stated that impropriety does not depend on the offender's consciousness of impropriety. Impropriety:

'...is not restricted to an abuse of power. It may consist of the doing of an act which a director or officer knows or ought to know that he has no authority to do.'

Based on these interpretations, and bearing in mind that proof to the Briginshaw standard is required, his Honour found that the contraventions had been proven. The second, third and fourth defendants regarded the acquisition by CTC of the $6,000,000 as virtually amounting to funds for their own use. Each of the defendants had been involved in the contraventions for the purposes of s 79 of the Law.

(7) Banning orders

Having found that the Law had been contravened, banning orders pursuant to the Law were made. Foster AJ noted that section 1317EA(3)(a) of the Law (which has been replaced by section 206A of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482)) is designed to protect the public and to prevent the corporate structure from being used to the financial detriment of investors, shareholders, creditors, and persons dealing with the company. The defendants were banned from managing corporations for periods of between eight years and sixteen years.

(8) Pecuniary penalties

The contraventions were sufficiently serious to warrant the imposition of pecuniary penalties. In determining the amount of the pecuniary penalties, Foster AJ agreed with the plaintiff that the following factors should be taken into account:

- the defendants' conduct had resulted in the loss of over $3,000,000 from a public company and was deliberate and for their own personal gain;
- the defendants failed to show any contrition;
- the need to deter other directors from breaching directors' duties and other provisions presently found in the Corporations Act (general deterrence); and
- the need to punish the defendants for their conduct.

Pecuniary penalties ranging between $5,000 and $120,000 were imposed on the defendants.

(J) INTERIM REPORTS ON ASIC INVESTIGATIONS AND PROCEDURAL FAIRNESS
(By Steven Milesi, Corrs Chambers Westgarth)

Australian Securities and Investments Commission v Plymin (No 3) [2002] VSC 358, Supreme Court of Victoria, Mandie J, 28 August 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/vic/2002/august/2002vsc358.htm](http://cclsr.law.unimelb.edu.au/judgments/states/vic/2002/august/2002vsc358.htm%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

The Australian Securities and Investments Commission ("ASIC") must prepare an interim report of an investigation when it forms an opinion that a serious contravention of a law of the Commonwealth, or of a State or Territory, has been committed. But in what circumstances is ASIC deemed to have formed such an opinion, and does the availability of such a report, to a person whose affairs are addressed in it, create a necessity for procedural fairness during the investigative process?

In this case, in a proceeding for a civil penalty order brought by ASIC, the second defendant made an application to stay the proceeding, as an abuse of process of the Court, on the basis that he had not been accorded procedural fairness during the investigative process.

In support of the application the second defendant submitted that ASIC had breached its obligations under section 16(1) of the [Australian Securities and Investments Commission Act 1989 No. 90 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=6664" \t "default) (the "ASIC Act").

(1) Background

The principal proceeding before the Court was an insolvent trading proceeding against three directors of the Water Wheel group of companies ("Water Wheel") in which ASIC claimed civil penalties, compensation and disqualification orders.

An investigation was commenced in May 2000 into the affairs of Water Wheel and into a suspected contravention of section 588G of the then Corporations Law, as in operation in 1999 and early 2000.

Section 16(1) of the ASIC Act provides that ASIC must, where in the course of an investigation under Part 3 Division 1 of the ASIC Act it forms the opinion that a serious contravention of a law of the Commonwealth or a State or Territory has been committed, prepare an interim report that relates to the investigation. In such circumstances the interim report must set out findings about the contravention and the evidence and other materials on which the findings are based, as well as other matters relating to, or arising out of the investigation, as ASIC thinks fit.

Evidence in the proceeding was that during the course of the investigation, two of the individuals primarily responsible for the preparation of the proceeding, within ASIC's staff, believed that the second defendant's alleged contravention was a serious one.

In the proceeding commenced by ASIC on 27 November 2000, ASIC claimed, among other things, an order for a pecuniary penalty against the second defendant. Section 1317EA(5) of the former Corporations Law provided that a Court is not to make an order for a pecuniary penalty unless it is satisfied that the contravention is a "serious" one.

(2) Issues

The second defendant submitted ASIC had formed the opinion that a serious contravention of a law of a State had been committed but failed to prepare an interim report as required.

Section 18(3) provides that where a report, prepared in accordance with section 16(1) of the ASIC Act, relates to a person's affairs to a material extent, ASIC may, at the person's request or of its own motion, give to the person a copy of the report.

With reference to this section, the second defendant submitted he was entitled, by implication, to be informed of the existence of any interim report, because without knowledge of the existence of the report, section 18(3) of the ASIC Act would be nugatory. Accordingly, the second defendant submitted, ASIC's failure to prepare an interim report meant that he was necessarily unaware that ASIC had formed the opinion that he had committed a serious contravention. That breach resulted in procedural unfairness because it had deprived him of the opportunity to make submissions to ASIC in relation to the alleged contravention and the possible commencement of a proceeding in relation to it.

ASIC submitted there was no evidence proving directly or by inference that in the course of the investigation it had formed the opinion that a serious contravention had been committed.

ASIC further submitted the phrase "a law of the Commonwealth or a State or Territory" used in section 16(1)(a) of the ASIC Act did not cover a national law scheme. This submission was on the basis that the purpose of the provisions of section 16, as well as sections 17 and 18 of the ASIC Act, were to empower and require ASIC to report to other relevant authorities and agencies where any serious contravention of a law, other than a national law scheme, was identified. In cases involving contravention of a national law scheme, ASIC submitted that it had the authority itself to prosecute or otherwise deal with the contravention, and accordingly the provisions were inapplicable to this situation.

Thirdly, ASIC submitted that even in the event it had been obliged to prepare an interim report, its failure to do so did not give rise to a failure to accord procedural fairness to the second defendant, and finally, even if it did, there was no basis upon which the Court could permanently stay the proceedings as an abuse of process of the Court.

(3) Decision

(a) Forms an opinion

Mandie J interpreted the phrase "forms the opinion", as used in section 16(1)(a) of the ASIC Act, to mean that ASIC itself, or its delegate or officer if duly authorised to do so, should form the relevant opinion with an eye to that provision. His Honour referred to Deloitte Touche Tohmatsu v ASC (1994) 54 FCR 284, 290-291 and stated that in his opinion the correct construction of the phrase was that it denotes a formal and deliberate process of developing and formulating an opinion with an eye to the provision.

Mandie J found there was no evidence that ASIC had considered the formation of an opinion as to whether any contravention had been committed of sufficient seriousness to require it to prepare an interim report, let alone formed an opinion to that effect. His Honour held the fact that two of the ASIC staff in charge of the investigation and in charge of the preparation of this proceeding were of the belief that the alleged contravention was serious did not amount to the formation of an opinion by ASIC that a serious contravention had been committed for the purposes of section 16(1)(a).

Although Mandie J considered this finding was sufficient to dismiss the application, he went on to express his view on the other submissions.

(b) National scheme law

Mandie J was of the view the plain and ordinary meaning of the expression "a law of the Commonwealth or a State or Territory" should be taken to have been intended, and if Parliament had intended that national scheme laws should be excluded, this would have been expressly stated in the ASIC Act.

His Honour noted that in ASC v Solomon (1996) 19 ACSR 73, a decision of Tamberlin J in the Federal Court, ASIC's predecessor acted contrary to the submission it now advanced by relying on an interim report prepared under section 16(1)(a), on the basis that a serious contravention of the Corporations Law had been committed, for the purpose of seeking a winding up order.

(c) Procedural fairness

Mandie J expressed the opinion that the preparation of an interim report and the failure to prepare an interim report were irrelevant in law to the actual institution of the proceeding. His Honour considered section 16(1)(a) of the ASIC Act did not give rise to any special considerations of procedural fairness where none would otherwise arise.

Mandie J referred to relevant authorities on the issue of procedural fairness including The Medical Board of Queensland v Byrne (1958) 100 CLR 582, 591, 594; Barton v The Queen (1980) 147 CLR 75, 95; Commissioner of Police v Reid (1989) 16 NSWLR 453, 461; Cornall v A.B. [1995] 1 VR 372, 396-7, 400-401; Maxwell v The Queen (1996) 184 CLR 501, 512, 534, and said that, in general, procedural fairness does not extend to require that a proposed defendant must be afforded an opportunity to put submissions in relation to a decision to institute a prosecution or a like proceeding, such as a disciplinary proceeding. In the opinion of his Honour, this proceeding with its penal elements was strongly analogous to a proceeding such as a disciplinary hearing, if not a prosecution.

The view of Mandie J was that the statutory framework relevant to both the prior investigation and the proceeding did not afford any legitimate basis for contending that procedural fairness required any hearing prior to the trial of the proceeding itself.

(K) REMOVAL OF DIRECTORS BY SHAREHOLDERS - DOES THE CORPORATIONS ACT OVER-RIDE PROVISIONS IN A PUBLIC COMPANY'S CONSTITUTION?
(By Amber Cerny, Corrs Chambers Westgarth)

Allied Mining and Processing Ltd v Boldbow Pty Ltd [2002] WASC 195, Supreme Court of Western Australia, Roberts-Smith J, 26 July 2002

The full text of the judgment is available at:

[http://cclsr.law.unimelb.edu.au/judgments/states/wa/2002/july/2002wasc0195.html](http://cclsr.law.unimelb.edu.au/judgments/states/wa/2002/july/2002wasc0195.html%22%20%5Ct%20%22_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/%22%20%5Ct%20%22_new).

(1) Introduction

This recent decision of Roberts-Smith J in the Supreme Court of Western Australia provides a discussion of the methods available to shareholders for removing directors of companies. The decision analyses section 203D of the [Corporations Act 2001 No. 50 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=56482" \t "default) ("section 203D "). His Honour also discusses the tension between the shareholders right to remove directors and the directors right to natural justice.

(2) Facts

(a) Claim

The plaintiffs (Allied Mining & Processing Limited (ACN 002 594 872) ("Allied") and Mark Victor Caruso ("Caruso")) sought an order that the defendant (Boldbow Pty Limited ("Boldbow")) be restrained from proceeding to arrange or hold a general meeting of Allied in purported reliance on a notice of meeting dated 27 June 2002 sent to members of Allied on or about that date and also claimed damages and injunctive relief in relation to the proposed general meeting.

(b) Background

Caruso was a director of Allied. Allied was an ASX listed public company. Boldbow was a member of Allied holding more than 5% of the issued capital in Allied.

On 6 June 2002, Boldbow's solicitors wrote to Allied's directors:

(i) advising that Boldbow proposed to hold a general meeting of Allied's members in accordance with section 249F of the Corporations Act to consider resolutions to replace the existing board of directors;

(ii) requesting, under section 173(3) of the Corporations Act, a copy of Allied's register of members within 7 days; and

(iii) advising the current board that they should consider themselves as acting in a caretaker role pending the outcome of the general meeting and not enter into any transaction or take any action other than in the ordinary course of business.

On 7 June 2002, the plaintiff's solicitors responded to Boldbow's letter advising that the register of members would be provided and that Allied's board did not consider itself acting in a caretaker capacity.

Also on 7 June 2002, Allied announced a placement of 6,660,000 shares representing approximately 15% of Allied's issued share capital, and a one-for-five rights offer.

Allied's solicitors wrote to Boldbow's solicitors on 18 June 2002 enclosing a copy of Allied's register of members. They further advised that:

(a) the board of Allied had resolved to proceed with the placement;

(b) Boldbow had not complied with section 203D; and

(c) in the absence of confirmation that Boldbow intended to proceed with its intention to convene a members meeting, Allied was of the view that it was not in possession of any information which should be disclosed to the ASX under ASX Listing Rule 3.1.

Allied requested that if Boldbow intended to proceed with its proposal, a draft copy of the notice of meeting prior to dispatch to the shareholders be provided in order that Allied's board could provide notice, of the intention to move a resolution seeking the removal of a director from office, to the particular director or directors in question. The director or directors could include a written statement putting their case to members in the text of the notice of meeting and the solicitors could review the notice of meeting and explanatory material to confirm that none of the information included was defamatory in nature.

By a letter dated 21 June 2002, Boldbow's solicitors stated that Boldbow was not relying on section 203D but on article 21.8 of Allied's constitution which provided:

"The company may (in addition to any powers conferred by the Corporations Law) by Ordinary Resolution remove a Director (other than an Alternate Director) and by Ordinary Resolution appoint a person as a replacement Director but only where the Director the subject of the removal resolution, not less than five Business Days before notice of the General Meeting at which the resolution is to be considered is dispatched, has been given notice by the Company of the proposed resolution and, if in the period of three Business Days after the Director that has been given notice gives to the Board a written statement of not more than 1500 words relating to the proposed resolution, containing no defamatory material to the Company, a copy of that statement will be dispatched with the notice of the General Meeting at which the resolution is to be considered."

They also stated that even assuming the notification requirements in article 21.8 applied to a meeting convened by a shareholder pursuant to section 249F of the Corporations Act, (which they did not concede), in their submission those requirements were complied with by the delivery of their letter of 6 June 2002 which was addressed to the directors of Allied. They went on to say that notwithstanding that, if any of Allied's directors wished to provide material to Boldbow for circulation with Boldbow's notice of meeting, Boldbow would be happy to consider that request if the material was received by it by close of business on 24 June 2002.

There was subsequent correspondence between Allied's solicitors and Boldbow's solicitors where Allied argued that section 203D was the exclusive method for removing directors by an ordinary resolution and where Boldbow argued that it was entitled to proceed under article 21.8 of Allied's constitution as that provision and section 203D operated independently.

(3) Decision - Whether section 203D is the exclusive means or sets a minimum standard for shareholders to remove directors of a company

Section 203D provides for the removal of directors of public companies by members.

The issue considered by Roberts-Smith J was whether or not section 203D provided an exclusive procedure for the removal of directors.

Roberts-Smith J stated that section 203D sets a minimum standard for shareholders to remove directors of a company. He held that the purpose of the section is to prevent directors from becoming entrenched in their positions on the board of a company. He held further that even if a company's constitution contained provisions for the removal of directors, shareholders would have as a last resort recourse to section 203D.

In considering whether or not section 203D provided an exclusive procedure for the removal of directors Roberts-Smith J considered the judgments of Kenny JA in Link Agricultural v Shananhan (1998) 16 ACLC 1462 and Street J in Holmes v Life Funds of Australia Ltd (1971) 1 NSWLR 860.

In Link Agricultural v Shananhan and (1998) 16 ACLC 1462 Kenny JA held that where a company's constitution had a provision which outlined a procedure for removing directors by its members, neither that provision, nor section 227 of the Corporations Law (the equivalent of section 203D) prevented recourse to the other. Her Honour held that the two provisions created "concurrent and alternate procedures to which the company in general meeting may remove a director and appoint another in his place. The members have a choice."

Street J held in Holmes v Life Funds of Australia Ltd (1971) 1 NSWLR 860 that section 120 of the [Companies Act 1981 No. 89 (Cth)](http://www.lawlex.com.au/default.asp?pact=coredoc&nav=col&cid=7358" \t "default) was "not intended to provide a whole code for the removal of directors".

Roberts-Smith J stated that section 203D could never be excluded but could be "supplemented by constitutional articles providing alternative ways, whether more or less rigorous than section 203D, by which shareholders may remove directors."

His Honour concluded that while there is a tension between preventing directors from becoming entrenched in their positions on the boards of companies and the shareholders power to remove directors on the one hand and the director's right to natural justice when shareholders seek to remove those directors on the other, the tension is to be resolved in favour of the shareholders.

For the above reasons, Roberts-Smith J found for the defendant and dismissed the plaintiffs' claim.

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