|  |
| --- |
| **Important notice:** You may use this material for your own personal reference only. The material may not be used, copied or redistributed in any form or by any means without a LAWLEX enterprise wide subscription.  **Corporate Law Bulletin**  **Bulletin No. 92, April 2005**  Editor: [Professor Ian Ramsay](mailto:i.ramsay@unimelb.edu.au), Director, Centre for Corporate Law and Securities Regulation  Published by [LAWLEX](http://www.lawlex.com.au" \t "default) on behalf of [Centre for Corporate Law and Securities Regulation](http://cclsr.law.unimelb.edu.au" \t "_new), Faculty of Law, the University of Melbourne with the support of the [Australian Securities and Investments Commission](http://www.asic.gov.au" \t "_new), the [Australian Stock Exchange](http://www.asx.com.au" \t "_new) and the leading law firms: [Blake Dawson Waldron](http://www.bdw.com.au" \t "_new), [Clayton Utz](http://www.claytonutz.com" \t "_new), [Corrs Chambers Westgarth](http://www.corrs.com.au" \t "_new), [Freehills](http://www.freehills.com" \t "_new), [Mallesons Stephen Jaques](http://www.mallesons.com" \t "_new), [Phillips Fox](http://www.phillipsfox.com" \t "_new).  ***Use the arrows to navigate easily across the bulletin***= back to Brief Contents = back to top of current section |
| **Brief Contents** |
| |  |  |  |  | | --- | --- | --- | --- | |  |  |  |  | | **1.** | [**Recent Corporate Law and Corporate Governance Developments**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#h1) | **7.** | [**Subscription**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#7) | | **2.** | [**Recent ASIC Developments**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#h2) | **8.** | [**Change of email address**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#8) | | **3.** | [**Recent ASX Developments**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#h3) | **9.** | [**Website version**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#9) | | **4.** | [**Recent Takeovers Panel Developments**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#h4) | **10.** | [**Copyright**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#10) | | **5.** | [**Recent Corporate Law Decisions**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#h5) | **11.** | [**Disclaimer**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#11) | | **6.** | [**Contributions**](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#6) |  |  | |  |  |  |  | |
| **Detailed Contents** |
| **[1. Recent Corporate Law and Corporate Governance Developments](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm" \l "1)**  [1.1 Independent expert reports: are they independent, and are they expert?](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#011) [1.2 Directors' duties and corporate social responsibility](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#012) [1.3 First jail terms following the collapse of HIH Insurance](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#013) [1.4 US Business Roundtable views on Sarbanes-Oxley Act section 404](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#014) [1.5 SEC charges the New York Stock Exchange with failing to Police specialists](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#015) [1.6 Non-executive director remuneration study](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#016) [1.7 APRA releases Basel II approach to credit risk](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#017)  [1.8 Final communiqué of the 30th annual conference of the International Organization of Securities Commissions](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#018)  [1.9 SEC issues guidance regarding prohibited conduct in connection with IPO allocations](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#019) [1.10 Report on rehabilitating large companies in financial difficulties](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0110) [1.11 Study of board turnover](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0111) [1.12 Corporate responsibility index](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0112) [1.13 NASD endorses concise, web-based point of sale mutual fund disclosure](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0113) [1.14 Superannuation investment in infrastructure](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0114) [1.15 FSA and industry propose rules on soft commissions and bundled brokerage](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0115) [1.16 Europe's approach to risk management and internal control](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0116)  [1.17 CESR report on credit rating agencies](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0117)  [1.18 UK laws on corporate manslaughter](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0118) [1.19 CEBS starts consultation on supervisory disclosure](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0119) [1.20 Australian financial stability review](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0120) [1.21 Global corruption report](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0121) [1.22 Research report: employee share ownership schemes](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0122)  **[2. Recent ASIC Developments](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm" \l "2)**  [2.1 ASIC further extends interim relief for managed investment scheme constitutions](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#021) [2.2 Changes to financial reporting relief for wholly-owned entities](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#022)  **[3. Recent ASX Developments](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm" \l "3)**  [3.1 Changes to the arrangements for the National Guarantee Fund (NGF)](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#031)  [3.2 Miscellaneous amendments to the ASIC settlement rules](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#032) [3.3 Miscellaneous amendments to the ACH clearing rules](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#033)  **[4. Recent Takeovers Panel Decisions](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm" \l "4)**  [4.1 National Foods Limited 01: Panel concludes proceedings](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#041)  **[5. Recent Corporate Law Decisions](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm" \l "5)**  [5.1 Extension of time provisions to be given a liberal construction](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#051) [5.2 Schemes of arrangement: Inadequate disclosure](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#052) [5.3 Are directors parties to a directors and officers insurance contract?](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#053)  [5.4 Provision in constitution of company whereby a member ceases to be a member if he becomes bankrupt](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#054) [5.5 Interpretation of the civil penalty provisions of the Corporations Act](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#055) [5.6 Shareholder cannot sue for loss that is merely reflective of loss suffered by company](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#056) [5.7 Entry into loan facility not an unconscionable transaction](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#057) [5.8 Application for termination of winding-up order under section 482](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#058)  [5.9 Construction of costs enforcement clause in mining royalty agreement](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#059) [5.10 Provisions in Corporations Act dealing with independence of auditors can affect claim for legal professional privilege](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0510)  [5.11 Voting by a secured creditor who has failed to estimate the value of their security may lead to surrender of the entire security](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0511) [5.12 Liquidators' unsuccessful attempt to disclaim contracts](http://www.law.unimelb.edu.au/bulletins/LAWLEX-old-editions/LAWLEX%20Corporate%20Law%20Bulletin%20No%2092%20%28April%202005%29.htm#0512) |
| **1. Recent Corporate Law and Corporate Governance Developments** |
| **1.1 Independent expert reports: are they independent, and are they expert?**  By Elizabeth Bennett, Lawyer and Jon Webster, Partner, Allens Arthur Robinson (Jon Webster is co-author of the book Experts’ Reports in Corporate Transactions, Federation Press ([http://www.federationpress.com.au/bookstore/book.asp?isbn=1862874697](http://www.federationpress.com.au/bookstore/book.asp?isbn=1862874697" \t "_new))  The heightened activity in corporate takeovers has led to a greater focus on the role and value of independent experts in major transactions. In the present corporate regulatory climate, company directors are increasingly looking to independent experts to play a central role in supporting their view of the value of their company. In this context, there has been some disquiet over the quality and independence of expert reports.  Independent experts’ reports can be required under the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) or the ASX Listing Rules. Directors of a company can also voluntarily commission a report, as commonly occurs in response to a hostile takeover bid. Mandatory and voluntary reports have a common aim of providing a measure of protection for investors without the skills or resources to conduct an analysis of the value of a company themselves.  This is a role of considerable importance in a market in which shares in large and complicated companies are widely held by retail investors. A high profile example of the importance that can be attached to the view of an independent expert is Grant Samuel's expert report that was so pivotal in the recent battle for WMC. Grant Samuel's view that $6.35 a share did not represent 'fair value' for shares in WMC was a major weapon in the WMC arsenal against Xstrata. Similarly, BHP's bid in the upper half of the independent valuation was a key part of its warm reception by the market.  **(a) Issues**  In this climate, two key issues have emerged: First, there is a growing perception that independent experts are not, in the true sense, independent. Second, the expert reports themselves are of varying quality, often containing superfluous and confusing information. Given the increasing importance of expert reports in the takeover context, these are matters of concern. This concern has been reflected in ASIC's recent policy proposal, which seeks input into the adequacy and value of expert reports.  **(b) Independence**  An expert cannot be 'associated with' a party to the transaction. The word 'independent' in this context is protected by section 923A(2) of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default), and the relevant misleading and deceptive provisions in the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default). However, there is concern that the present tests are inadequate, in light of the narrow range of specialists available to provide the services of an independent expert.  Some commentators have noted that, in the truest sense, no expert report can be "independent" where it has been commissioned by one party, particularly where there is a clear agenda, such as defeating a takeover bid. Suggestions for addressing this issue include requirements that parties affected by an independent report contribute some funding to a report. Under such a regime, WMC and Xstrata would have shared the cost of the Grant Samuel Report in the recent takeover bid. While in some ways this is an attractive option, the fact remains that requiring both parties to consent to and fund an independent report will not always be a realistic option, particularly in an acrimonious takeover bid.  An alternative suggestion has been the imposition of a fiduciary relationship between the expert and the commissioning company. The imposition of such a standard would create higher obligations for an expert to avoid conflicts and undisclosed profits. A fiduciary must act at all times in the interest of the person to whom the obligation is owed. But the imposition of a fiduciary obligation would be inconsistent with the very concept of 'independence'.  There is the further issue of whether or not a general commercial association between a commissioning company and an independent expert will necessarily compromise independence. In the past, the Courts have recognised the commercial reality that an expert in the market will not necessarily lack independence, merely by reason of having provided services in the past, depending on the services that were provided.  Nonetheless, ASIC has sought comment on methods by which independence could be protected further, through the control of conflicts.  **(c) Quality of expert reports**  It must be recognised that conflict control mechanisms may have an impact beyond independence alone. Conflict control, by its nature, operates to exclude certain parties from acting as experts. Often, these are advisors with a background working with the commissioning company.  In precluding such companies from providing reports, there is concern that some expert reports lack the necessary skill and knowledge in the relevant market to make authoritative statements that are of value to investors. In addition, the often technical nature of the reports that experts are required to provide can be obscured by the inclusion of superfluous technical information. Where there is only a small and confined market for the provision of these services, it is more difficult to be certain that an independent and competent expert is available in the relevant field. Given the dual issue of quality and independence, there may be scope to license experts, either generally, or in a particularly complex field. ASIC's ability to revoke an expert's licence may provide the necessary incentive to raise professional standards.  However, more fundamentally than this, there is a need for these issues to be confronted at the practical level by those who commission and provide the expert reports. In this regard, the push by ASIC for companies providing expert reports to be more aware of the protocols in place to protect independence is both welcome and necessary.  There is little doubt that expert reports are an important and desirable safeguard for the market in general. However, the concerns relating to the quality and independence of the reports must be addressed if their true value is to be realised.  **1.2 Directors’ duties and corporate social responsibility**  In the March 2005 issue of this Bulletin, it was mentioned that the Parliamentary Secretary to the Treasurer, the Hon Chris Pearce MP, has asked the Corporations and Markets Advisory Committee (CAMAC) to investigate possible reform of directors’ duties as part of the Government’s response to the Special Commission of Inquiry into the actions of James Hardie Industries.  The specific questions that have been referred to CAMAC have now been made available. The questions are:  1. Should the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) be revised to clarify the extent to which directors may take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions?  2. Should the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) be revised to require directors to take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions?  3. Should Australian companies be encouraged to adopt socially and environmentally responsible business practices and if so, how?  4. Should the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) require certain types of companies to report on the social and environmental impact of their activities?  An article in The Age newspaper discusses the inquiry by CAMAC. The article is at: [http://www.theage.com.au/news/Stephen-Bartholomeusz/New-director-plans-could-backfire/2005/04/05/1112489485068.html](http://www.theage.com.au/news/Stephen-Bartholomeusz/New-director-plans-could-backfire/2005/04/05/1112489485068.html" \t "_new)  **1.3 First jail terms following the collapse of HIH Insurance**  When HIH Insurance Limited (HIH) collapsed in 2001, it was Australia’s biggest corporate collapse, with losses of $5.3 billion. The first two jail terms have now been imposed on former officers of HIH Insurance.  **(a) Ray Williams**  On 15 April 2005 Ray Williams, the former Chief Executive Officer of HIH was sentenced to four-and-a-half years' jail with a non-parole period of two years and nine months. Mr Williams was convicted and sentenced on three criminal charges arising from his management of the HIH group of companies in the three-year period 1998 to 2000. Mr Williams was sentenced in relation to offences concerning three substantial transactions, which significantly distorted the true financial position of HIH.  Mr Williams was sentenced after pleading guilty on 15 December 2004 to three criminal charges:   * that he was reckless and failed to properly exercise his powers and discharge his duties for a proper purpose as a director of HIH Insurance Limited when, on 19 October 2000, he signed a letter that was misleading; * that he authorised the issue of a prospectus by HIH on 26 October 1998 that contained a material omission; and * that he made or authorised a statement in the 1998-99 Annual Report, which he knew to be misleading, that overstated the operating profit before abnormal items and income tax by $92.4 million.   Mr William's sentencing on the three criminal charges follows ASIC's successful civil penalty proceedings (commenced in 2001) that resulted in him being:   * banned from acting as a director of any company for 10 years; * ordered to pay compensation jointly with Mr Rodney Adler and Adler Corporation Pty Limited of approximately $7 million; and * ordered to pay a pecuniary penalty of $250,000.   **(b) Rodney Adler**  On 14 April 2005 Mr Rodney Adler, a former director of HIH, was sentenced to four-and-a-half years' jail, with a non-parole period of two-and-a-half years, on four charges arising from his conduct as a director of the HIH group of companies in 2000.  Mr Adler was sentenced after pleading guilty on 16 February 2005 to four criminal charges:   * two counts of disseminating information on 19 and 20 June respectively, knowing it was false in a material particular and which was likely to induce the purchase by other persons of shares in HIH contrary to section 999 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default); * one count of obtaining money by false or misleading statements, contrary to section 178BB of the [Crimes Act 1900 (NSW)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=3907" \t "default); and * one count of being intentionally dishonest and failing to discharge his duties as a director of HIH in good faith and in the best interests of that company contrary to section 184(1)(b) of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default).   The sentencing of Mr Adler follows ASIC's successful civil penalty proceedings against him, which were commenced in 2001 and resulted in him being:   * disqualified from acting as a director of any company for 20 years; * ordered to pay compensation jointly with Adler Corporation Pty Limited and Mr Ray Williams of approximately $7 million; and * ordered to pay a pecuniary penalty of $450,000. Adler Corporation Pty Limited was also ordered to pay a pecuniary penalty of $450,000.   **(c) Ongoing prosecutions**  ASIC's HIH investigation has already led to criminal prosecutions of 9 former senior executives, including directors, of FAI, HIH and associated entities on 31 [Corporations](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and [Crimes Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=3907" \t "default) charges. These criminal prosecutions include:   * On 23 December 2003, Mr William Howard, a former General Manager of HIH Insurance Limited, was sentenced to three years imprisonment, fully suspended on the basis of on-going assistance to the HIH investigation. Mr Howard had pleaded guilty to two counts of criminal misconduct, namely that he dishonestly received from Mr Brad Cooper approximately $124,000 in return for facilitating payments by HIH directly or indirectly in favour of Mr Cooper. Mr Howard also admitted facilitating a payment of $737,000 to a company associated with Mr Cooper knowing that the payment obligation had already been discharged; * On 22 October 2004, Mr Bradley Cooper was committed for trial on six charges of corruptly giving a cash benefit to influence an agent of HIH Insurance Limited, namely Mr Howard, and seven charges of publishing a false or misleading statement with intent to obtain financial advantage. The trial is set down to commence on 1 August 2005; * On 20 April 2004, Mr Charles Abbott, the former Deputy Chairman of HIH Insurance Limited, was charged with dishonestly using his position as a company director. The committal hearing is set down to commence on 30 May 2005; * On 19 July 2004, Mr Timothy Maxwell Mainprize was committed for trial on charges of failing to act honestly in the exercise of his powers and discharge of his duties as an officer of FAI General Insurance Company Limited. He was also committed on one count of providing false and misleading information. His trial is set down to commence on 5 September 2005; * On 19 July 2004, Mr Daniel Wilkie was committed for trial on charges of failing to act honestly in the exercise of his powers and discharge of his duties as an officer of FAI General Insurance Company Limited. He was also committed on one count of providing false and misleading information. His trial is set down to commence on 5 September 2005; * On 19 July 2004, Mr Stephen Burroughs was committed for trial on charges of failing to act honestly in the exercise of his powers and discharge of his duties as an officer of FAI General Insurance Company Limited; and * On 24 March 2005 Mr Terry Cassidy pleaded guilty to two charges of recklessly making false statements and one charge of recklessly failing to discharge his duties as a director for a proper purpose. There sentencing hearing commenced on 19 April 2005.   The above information has been drawn from ASIC media releases dated 14 April 2005 and 15 April 2005.  **1.4 US Business Roundtable views on Sarbanes-Oxley Act section 404**  One of the most controversial parts of the US Sarbanes-Oxley Act is section 404 which deals with management’s report on internal control over financial reporting and the auditor’s attestations related thereto.  On 13 April 2005, in testimony at a Securities and Exchange Commission (SEC) roundtable on implementation of the Sarbanes-Oxley Act section 404, the US Business Roundtable reaffirmed its support for the principles of the Sarbanes-Oxley Act, and provided the SEC and the Public Company Accounting Oversight Board (PCAOB) with recommendations for improving section 404’s efficiency and effectiveness while preserving the law’s intended benefits.  The Business Roundtable is an association of CEOs of 160 leading US companies.  The Business Roundtable stated: “Clearly, the result of the 404 process has been as Congress intended with improved investor confidence in our capital markets. While Roundtable companies continue to support Sarbanes-Oxley and the underlying premise of section 404, in the implementation process thus far, the benefits of 404 have not always outweighed the burdens.”  The Business Roundtable outlined some of the challenges of section 404 for large public companies, most notably increasing costs and human resources the reallocation of which, it noted, had forced numerous companies to “put market opportunities and innovation on hold.” A recent Business Roundtable survey found that 47% of responding companies estimated costs of more than US$10 million, up from 22% in 2004.  Several recommendations were submitted by the Business Roundtable to improve implementation of section 404 and Auditing Standard No 2, the PCAOB’s standard for use by auditors to assess companies’ financial statements in compliance with section 404 including:  **(a) Change in tone**  In response to heightened scrutiny, public companies have taken a conservative approach to implementing Accounting Standard No 2, which has increased 404’s costs. The SEC and PCAOB could convey clearly to public companies’ accounting firms that they may exercise their professional judgment and use flexibility in applying Auditing Standard No 2.  **(b) Greater latitude in testing and “Walkthroughs”**  The 404 process could be enhanced if management and the auditor are given greater latitude to use judgment in determining which key controls need to be tested, and are permitted to conduct “walkthroughs” for only a random sampling, rather than all, of the major classes of transactions in a given year.  **(c) Professional judgment in relying on work of others**  Auditing Standard No 2 could be revised to clarify that the independent auditor is encouraged to exercise its professional judgment and rely on the work of others as principal evidence in appropriate circumstances.  The Business Roundtable submission is available at: [http://www.businessroundtable.org/pdf/20050413000SECRoundtable-LettertoSEC-4.13.05.pdf](http://www.businessroundtable.org/pdf/20050413000SECRoundtable-LettertoSEC-4.13.05.pdf" \t "_new)  **1.5 SEC charges the New York Stock Exchange with failing to police specialists**  On 12 April 2005 the United States Securities and Exchange Commission (SEC) instituted and simultaneously settled an enforcement action against the New York Stock Exchange, Inc., finding that the NYSE, over the course of nearly four years, failed to police specialists, who engaged in widespread and unlawful proprietary trading on the floor of the NYSE. The Commission found that the NYSE violated section 19(g) of the Securities Exchange Act of 1934 by failing to enforce compliance with the federal securities laws and NYSE rules which prohibit specialists from "interpositioning" and "trading ahead" of customer orders.  In settling this action, the NYSE consented, without admitting or denying the findings, to entry of an order imposing a censure and requiring the NYSE to cease and desist from future violations of the federal securities laws. The NYSE also agreed to several significant remedial measures designed to strengthen the NYSE's oversight of specialists and other floor members. The NYSE agreed to an undertaking of US$20 million to fund regulatory audits of the NYSE's regulatory program every two years through the year 2011. The NYSE has also agreed to implement a pilot program for video and audio surveillance on its trading floor for at least an eighteen-month period.  Specifically, the Commission's Order finds that from 1999 through 2003, various NYSE specialists repeatedly engaged in unlawful proprietary trading, resulting in more than US$158 million of customer harm. The improper trading took various forms, including "interpositioning" the firms' dealer accounts between customer orders and "trading ahead" for their dealer accounts in front of executable agency orders on the same side of the market. From 1999 through almost all of 2002, the NYSE failed to adequately monitor and police specialist trading activity, allowing the vast majority of this unlawful conduct to continue. The illegal trading went largely undetected because the NYSE's regulatory program was deficient in surveilling, investigating and disciplining the specialists' trading violations.  More information is available at: [http://www.sec.gov/news/press/2005-53.htm](http://www.sec.gov/news/press/2005-53.htm" \t "_new)  **1.6 Non-executive director remuneration study**  On 11 April 2005 a new report on non-executive director remuneration was published.  The study examines remuneration paid to non-executive directors and chairmen of the largest 200 Australian Stock Exchange companies. The study was prepared by Corporate Governance International.  Part 1 of the report examines the rates and structure of pay in 2004 for non-executive directors (NEDs) from a sample of 105 ASX200 listed entities. Part 2 of the report examines how NED pay could be structured, including appropriate pay rates, for the job involved.  Part 2 also looks at where NEDs currently tend to be drawn from, whether that pool needs to be deepened, how the selection process for NEDs can be made more transparently effective and how NEDs can demonstrate better that they are, in fact, performing the role of a competent board and worth their substantial pay.  According to the report, for the top 20 companies, the average remuneration for chairmen was $373,000 and the average remuneration for NEDs was $156,870.  For the top 20-50 companies, the average remuneration for chairmen was $302,976 and the average remuneration for NEDs was $120,296.  For the top 50-100 companies, the average remuneration for chairmen was $215,768 and the average remuneration for NEDs was $93,436.  For the top 100-200 companies, the average remuneration for chairmen was $143,446 and the average remuneration for NEDs was $74,087.  The full report is available on the Corporate Governance International website at: [http://www.cgi.au.com](http://www.cgi.au.com" \t "_new) under “Research Papers”.  **1.7 APRA releases Basel II approach to credit risk**  On 11 April 2005 the Australian Prudential Regulation Authority (APRA released the first of a series of discussion papers on the implementation of the new Basel II capital adequacy regime, known as the Basel II Framework, in Australia. The paper deals with the ‘standardised’ approach to credit risk and proposes a new prudential standard in this area.  Most Australian banks, building societies and credit unions are likely to adopt the standardised approach to determine their regulatory capital requirements for credit risk. However, APRA expects larger banks, which in aggregate represent the majority of assets in the industry, to seek accreditation for the more sophisticated Basel II approaches. Prudential standards for these approaches will be issued for consultation shortly.  A full suite of prudential standards for the Basel II Framework will be released for consultation in coming months. APRA expects to issue a final version in early 2007, which will then be tabled in Parliament, and the new capital adequacy regime will come into force on 1 January 2008. The qualitative risk management requirements under the Basel II Framework will also be included in a single prudential standard on risk management, for release by APRA in 2006.  The discussion paper and draft standard, including the discretions APRA intends to exercise for the standardised approach to credit risk, are available on the APRA website at: [http://www.apra.gov.au/ADI/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=8504](http://www.apra.gov.au/ADI/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=8504" \t "_new) and [http://www.apra.gov.au/Policy/Draft-Prudential-Standards-and-Guidance-Notes-for-Authorised-Deposit-Taking-Institutions.cfm](http://www.apra.gov.au/Policy/Draft-Prudential-Standards-and-Guidance-Notes-for-Authorised-Deposit-Taking-Institutions.cfm" \t "_new)  Comment on the documents is due no later than 30 September 2005. APRA has also finalised the majority of the discretions it intends to exercise for the internal rating-based (IRB) approach to credit risk and for securitisation. These are available on APRA’s website at: [http://www.apra.gov.au/ADI/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=8502](http://www.apra.gov.au/ADI/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=8502" \t "_new)  **1.8 Final communiqué of the 30th annual conference of the International Organization of Securities Commissions**  On 7 April 2005 the International Organization of Securities Commissions (IOSCO) released its final communiqué arising from its 30th annual conference held in Colombo, Sri Lanka, from 4 to 7 April 2005. This year's conference attracted more than 400 delegates from around the world and included representatives from more than 100 jurisdictions.  The matters the communiqué deals with include:   * IOSCO strategic direction; * dealing with uncooperative jurisdictions; * financial fraud; * code of conduct for rating agencies; * accounting, auditing and disclosure; * regulation of securities markets; * regulation of market intermediaries; * enforcement and exchange of information; and * investment management.   The communiqué is available at: [http://www.iosco.org/news/pdf/IOSCONEWS88.pdf](http://www.iosco.org/news/pdf/IOSCONEWS88.pdf" \t "_new)    **1.9 SEC issues guidance regarding prohibited conduct in connection with IPO allocations**  On 7 April 2005 the United States Securities and Exchange Commission issued an interpretive release (Release Nos. 33-8565; 34-51500; IC-26828) to provide guidance regarding prohibited conduct by underwriters in connection with initial public offering (IPO) allocations.  Regulation M prohibits underwriters and others from bidding for, purchasing, or attempting to induce any person from bidding for or purchasing an offered security during a restricted period as defined in Regulation M. Generally, the restricted period begins 1 or 5 business days prior to the determination of an offering price and ends upon a person's completion of participation in the distribution.  The guidance serves as a reminder that attempts to induce aftermarket purchases during a restricted period are prohibited by Regulation M. Attempts to induce aftermarket bids or purchases undermine the integrity of the market as an independent pricing mechanism and give prospective IPO purchasers the impression that there is a scarcity of the offered securities and the balance of their buying interest can only be satisfied in the aftermarket. Moreover, other investors who purchase shares in the aftermarket would not know that aftermarket demand had been stimulated by the underwriter's unlawful conduct. The guidance includes references to recent Commission enforcement cases alleging inducements in the offering process in violation of Regulation M.  The guidance also discusses distinctions between conduct that violates Regulation M and legitimate book-building.  The Commission solicits comments on the guidance for its consideration as it continues to monitor IPO allocation practices.  Further information is available on the SEC website at: [http://www.sec.gov/news/press/2005-49.htm](http://www.sec.gov/news/press/2005-49.htm" \t "_new)  **1.10 Report on rehabilitating large companies in financial difficulties**  On 7 April 2005 the Corporations and Markets Advisory Committee (CAMAC) released its report on rehabilitating large and complex enterprises in financial difficulties.  While supportive of the voluntary administration procedure for companies in financial difficulty, the Advisory Committee proposes some changes in the relevant legislation. It does not support adoption of a system of corporate recovery based on Chapter 11 of the US Bankruptcy Code.  Voluntary administration (VA) has become the principal corporate rehabilitation procedure since its introduction into the Corporations Act in 1993. It has been used for various large and complex enterprises, including Ansett and Pasminco, as well as for numerous small and medium enterprises. In light of this experience, the Government requested the Advisory Committee to consider the following questions.  Are there any particular difficulties in applying Part 5.3A to large and complex enterprises?  The Advisory Committee has not identified any fundamental difficulties in applying the VA provisions to large and complex enterprises, or any circumstances where it is necessary to have separate corporate recovery regulation for these enterprises.  Should a new system of corporate rehabilitation along the lines of chapter 11 of the United States Bankruptcy Code be adopted in Australia?  The report does not recommend adoption of US Chapter 11. The Advisory Committee finds no compelling need or intrinsic shortcoming in the VA procedure, that would call for a new system of corporate rehabilitation along the lines of US Chapter 11. There was overwhelming support in submissions for retaining VA, and not adopting Chapter 11 as an additional or substitute corporate recovery procedure. A US 'debtor in possession' model – under which directors of a company in financial stress are left in control - could not be introduced in Australia without fundamental changes to the rehabilitation process and the role of the courts, for which there is no apparent demand.  Are there any particular changes required to Part 5.3A better to accommodate large corporate rehabilitation cases?  While finding Part 5.3A to be fundamentally sound, the Advisory Committee recommends changes to improve its workability for larger, as well as other, enterprises. Some of the proposed changes (for instance, timing of creditors' meetings) are more likely to arise in the administration of large and complex enterprises, while others (for instance, rights of substantial chargees) may arise in any type of administration.  The recommended changes include:  **(a) Substantial chargees appointing a receiver**  Currently, a substantial chargee (a creditor with a charge over the whole or substantially the whole of a company's property) has 10 business days from the time of being notified of the administrator's appointment to decide whether to appoint a receiver. This limited decision period may prompt substantial chargees to exercise their appointment powers prematurely, thereby unnecessarily undermining the prospect of a successful corporate recovery. The Advisory Committee proposes extending the initial decision period to 15 business days and also allowing an administrator and a substantial chargee to agree that a receiver can be appointed after that period.  **(b) Financing**  The ability of a company under administration to obtain further working capital can be a key element in its successful recovery. The Advisory Committee proposes to assist that process by permitting existing unsecured creditors (by three quarters by value and a simple majority by number of those who vote) to give a new financier priority over their own interests.  **(c) Who can be an administrator?**  The class of persons eligible to be an administrator should be widened to cover any insolvency practitioner, lawyer or other person with adequate corporate rehabilitation expertise and experience. Conversely, mere registration as a liquidator should not suffice.  **(d) Administrator's casting vote**  The Committee proposes retaining the right of an administrator to exercise a casting vote where there is a deadlock between the vote of creditors by value and by number. However, administrators should be required to publish their reasons for exercising any casting vote, which will reinforce their accountability to creditors.  **(e) Electronic communication**  An administrator may incur considerable costs in having to communicate with creditors in writing. The report proposes giving an administrator greater discretion to communicate electronically with creditors, while still ensuring that all information is available to them.  **(f) Pooling**  The report puts forward a series of recommendations to permit corporate group companies in VA to adopt a unified administration and enter into a single deed of company arrangement.  Other recommended changes include:   * increase the time for holding first and major meetings; * permit a committee of creditors to approve an administrator's remuneration; * allow a corporation to be a member of a committee of creditors; * streamline the disclosure requirements in an equity for debt offer to creditors; and * give liquidators at least one year from the date of their appointment to commence litigation to undo voidable transactions.   Are there any particular changes required to Part 5.1 arrangements and reconstructions to accommodate large corporate rehabilitation cases?  The Advisory Committee does not propose any changes to the creditors' schemes of arrangement provisions to accommodate large and complex enterprises.  Copies of the report are available on the CAMAC website at: [http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2004/$file/Large\_Enterprises\_report\_Oct04.pdf](http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2004/$file/Large_Enterprises_report_Oct04.pdf" \t "_new)  **1.11 Study of board turnover**  Analysis of board turnover in the largest 200 Australian Stock Exchange (ASX) companies over the past 4 years has revealed a modest but steady renewal of the Australian non-executive director (NED) ‘gene’ pool, according to a report published on 5 April 2005.  The analysis, by Proxy Australia, has shown that whilst new blood is slowly entering the director pool, existing ASX 200 directors are 4.4 times more likely than prospects without a current board seat to be chosen to fill a vacancy.  **(a) Methodology**   * The study examined board turnover in 138 companies that were continuously present in the ASX 200 during the period 2001 - 2004; * The analysis, covering 1,125 directors, identified board changes as a result of the addition of new directors, or the departure of existing directors; and * The study distinguished between directors that were new entrants to ASX 200 board positions and those directors who had concurrent ASX200 directorships.   **(b) Key findings**   * The average board studied turned over 15.8% of its non-executive directors each year (roughly one of seven NEDs per annum) between 2001 and 2004. If this trend continues this suggests that the average board will renew itself entirely once every seven years; * An average of 11.46% of ASX 200 companies turned over their CEO between 2001–2003. CEO tenure has been estimated at 5.6 years. (Source, Booz Allen Hamilton/ BCA CEO Tenure Study, 23 November 2004); * Director turnover peaked in 2003 at 19.18% (nearly one in five NEDs per annum), presumably as a result of the introduction of the ASX Corporate Governance Guidelines; * 62% of all non-executive director appointments in 2002 and 2003 came from directors with no other ASX 200 board seat. However over the entire period, candidates from ‘inside’ the existing ASX 200 director pool were 4.4 times more likely to be chosen to fill a vacant position than those outside the pool; * However, the portion of ‘new blood’ entering the ASX 200 director ‘gene pool’ seems on the decline. In 2004 the percentage of non-executive directors appointed without another ASX 200 board seat had declined to 51%. Thus in 2004 a candidate ‘inside’ the existing pool of NEDs were 6 times more likely to fill a vacant position than a candidate outside the pool; * Pay rates for non-executive directors experienced a sharp increase in the period observed. Excluding chairmen, NED pay rose on average from $80,541 in 2001 to $103,077 in 2004 a net increase of 28% over the period; and * New appointments to the ranks of Australia’s top companies were more likely to be independent than in the past. An average of 79.8% of all new NED appointments were classed as independent according to IFSA guidelines over the period, compared to 70% for the total pool of NED’s in the companies studied.   **1.12 Corporate responsibility index**  On 4 April 2005, the results of the annual Corporate Responsibility Index were published. Westpac scored first place in the international benchmarking survey that measures corporate responsibility, maintaining its top ranking in the second Australian Corporate Responsibility Index while also outperforming 133 companies in the UK. In the Australian Index, Westpac is followed closely by BP, BHP Billiton, Rio Tinto and Toyota Australia.  A voluntary, self-assessment survey, the Corporate Responsibility Index sets up a process that compares the systems and performances of different companies in and across specific sectors. Its primary focus areas are strategy, integration, management practice and performance and impact. The Index was established three years ago by over 80 businesses working with UK charity Business in the Community (BITC).  Twenty-seven companies participated in the second Australian Corporate Responsibility Index, ranging from the finance sector to manufacturing to extractive industries. Ernst & Young’s Environment & Sustainability Services team validated all submissions, a process that ensured that all survey answers were supported by substantiating evidence. This process usually led to further discussions and requests for additional information and some site visits.  Further information about the Index and the full ranking of all participating companies is available at [http://www.corporate-responsibility.com.au/results/2004\_results.asp](http://www.corporate-responsibility.com.au/results/2004_results.asp" \t "_new)  **1.13 NASD endorses concise, web-based point of sale mutual fund disclosure**  On 4 April 2005 the US National Association of Securities Dealers (NASD) recommended that the Securities and Exchange Commission (SEC) improve point of sale disclosure to mutual fund investors by mandating Internet disclosure of a new "Profile Plus", a two-page document providing basic information about a mutual fund, including its investment objectives, risks, performance, fees and expenses, and information about potential conflicts of interest.  NASD is also recommending that every broker-dealer be required to post a Profile Plus for each mutual fund it sells on the broker-dealer's website, with hyperlinks to the fund's prospectus and to a dealer disclosure statement with more information about the broker-dealer's potential conflicts of interest. Investors would also have the option of requesting paper delivery of the document.  Profile Plus is the chief recommendation of NASD's Mutual Fund Task Force in Mutual Fund Distribution, its second and final report to the SEC.  In its report, the task force also recommended that the SEC:   * update and modernize the findings that a fund board must make in approving and continuing a Rule 12b-1 plan; * list Rule 12b-1 fees in the prospectus fee table solely in a manner that describes their purpose, eg, as "distribution and shareholder servicing fees," without reference to a rule number that may be confusing to many investors; * mandate better disclosure to investors about the costs of Class B shares and, along with NASD, consider other regulatory issues concerning Class B shares; and * reconsider the unified fee proposal previously set forth by the SEC staff.   The work of the task force proceeded in two phases. Last November, the Task Force submitted its recommendations on Phase I in “The Report of the Mutual Fund Task Force on Soft Dollars and Portfolio Transaction Costs”. In Phase II, the task force focused on distribution arrangements, including 12b-1 fees and revenue sharing. Its recommendations are detailed in “Report of the Mutual Fund Task Force Mutual Fund Distribution”.  More information is available on the NASD website at: [http://www.nasd.com/](http://www.nasd.com/" \t "_new)  **1.14 Superannuation investment in infrastructure**  On 4 April 2005, the Parliament of Australia Library published a research note titled “Superannuation and investment in infrastructure”.  It is stated in the Introduction to the research note that the increase in the current account deficit has led to calls for increased spending on public infrastructure. The Deputy Governor of the Reserve Bank, Glenn Stevens, noted that capacity constraints in the rail network and ports were affecting Australia’s export performance, which may increase the current account deficit. As at the end of September 2004 total superannuation fund assets were about $648.9 billion, and net inflows to superannuation funds were about $5.8 billion a quarter. Easily, superannuation assets represent the largest group of funds available for investment. Against this background there have been calls for superannuation monies to be invested in infrastructure.  The research note looks at what is meant by the term ‘infrastructure’. The general guidelines that trustees must follow when making investment decisions are outlined and the advantages and disadvantages of superannuation funds investing in infrastructure considered. The many avenues for superannuation funds to invest in infrastructure are surveyed and possible barriers to investing in the sector are discussed.  The research note is available at: [http://www.aph.gov.au/Library/pubs/rn/2004-05/05rn42.pdf](http://www.aph.gov.au/Library/pubs/rn/2004-05/05rn42.pdf" \t "_new)  **1.15 FSA and industry propose rules on soft commissions and bundled brokerage**  On 31 March 2005 the UK Financial Services Authority (FSA) published for consultation rules addressing the issue of soft commissions and bundled brokerage arrangements. The rules, combined with proposals developed by industry, address the lack of transparency associated with soft commissions and should promote improved management of conflicts of interest.  The proposed rules confirm the FSA's position that fund managers' use of commission should be limited to the purchase of 'execution' and 'research' services (as set out in ‘PS04/23 on Bundled brokerage and soft commission arrangements: Update on issues arising from PS04/13’ published in November 2004). The consultation paper (CP05/5) also includes details of the work done by the fund management and broker sectors, with the involvement of pension fund trustees, in developing measures to enhance transparency and accountability in soft commission and bundled brokerage arrangements.  **(a) Proposed approach**  The proposed high-level rules, together with the industry proposals, will:   * limit investment managers’ use of dealing commission to the purchase of ‘execution’ and ‘research’ services; * require investment managers to disclose to their customers details of how these commission payments have been spent and what services have been acquired with them; * embed incentives to secure value for clients for execution and research expenditure in the commercial relationship between investment managers and brokers; and * promote a more level playing field in the production of research, whether within investment banks or by third parties.   The FSA paper sets out the services the FSA considers as legitimately falling within the definition of execution and research, which can therefore be paid for from commission under the new regime, and what it views as being non-permitted services. The FSA is proposing that non-permitted services include, amongst other things, computer hardware, seminar fees and travel or entertainment costs.  The FSA does not propose to state whether particular market pricing and information services are permitted or not but has set guidelines against which all services should be evaluated. The FSA will expect investment managers to apply these principles to determine whether particular goods and services they propose to acquire with commission are permitted services. They must be able to justify this decision to their clients and the FSA if asked.  **(b) Industry measures**  The FSA is satisfied that the industry's proposals are a credible way of addressing the lack of transparency and accountability that the FSA identified.  The proposals developed by the IMA, in conjunction with LIBA and NAPF, include:   * descriptions of investment managers' policies, processes and procedures in the management of trading commissions paid on behalf of clients; * client specific information on how commissions paid have been generated and how they have been used, including a split between amounts of commission spent on execution on the one hand and research on the other; * reports will be issued by fund managers to UK pension funds from Q1 2006 and to other UK funds from Q3 2006; and * the encouragement of forward-looking discussions between brokers and fund managers on how commission should be split between research and execution.   The FSA's consultation will close on 31 May with final rules being made in July 2005.  Bundling refers to the provision by brokers of other in-house services, such as research, together with dealing in securities in a single commission charge. Softing is the practice by which a broker agrees to pay for the supply of services from a third party to a fund manager in return for an agreed volume of business at an agreed commission rate. In both cases, the value of the services provided is dependent on how much business the fund manager places with the broker. The costs for these services are included in the commissions which are passed through by fund managers directly as charges to their clients.  **1.16 Europe’s approach to risk management and internal control**  In Brussels on 31 March 2005, at the launch of the discussion paper “Risk Management and Internal Control in the EU” the European Federation of Accountants (FEE), a representative organisation of the European Accountancy profession, stated that any new requirements to implement reporting on risk management and internal control must be based on evidence that the benefits to companies, shareholders and the public interest will exceed the costs involved.  FEE, the representative organisation of the European accountancy profession is calling for increased use of mechanisms to give more transparency to risk management, including:   * dialogue with shareholders; and * voluntary or required ‘comply or explain’ reporting against corporate governance requirements.   FEE is currently not convinced about the usefulness of introducing across the EU published effectiveness conclusions on internal control over financial reporting as required by section 404 of the Sarbanes-Oxley Act. However, it will be important to take account of the views of investors, companies and others, as well as forthcoming evidence about the usefulness, costs and benefits of such conclusions to investors as section 404 of the Sarbanes-Oxley Act is implemented.  The new FEE publication provides a review of current best practice amongst companies in risk management and internal control, a review of recent regulatory developments in the US and EU in response to the recent financial scandals; and a survey of regulatory requirements on risk management and internal control in EU member states.  The discussion paper Risk Management and Internal Control in the EU is available on the FEE website at: [http://www.fee.be](http://www.fee.be" \t "_new). Comments on the paper are invited by 31 July 2005.  Another relevant FEE publication in this area is the Discussion Paper on the Financial Reporting and Auditing Aspects of Corporate Governance (2003). It details the elements of good corporate governance relevant to the process of financial reporting and auditing and considers the fundamental relationships and obligations between the company boards, auditors, shareholders and other stakeholders in an effective corporate governance system.  **1.17 CESR report on credit rating agencies**  On 30 March 2005 the Committee of European Securities Regulators (CESR) published its report (ref CESR/05-139b) for the European Commission on possible measures concerning credit rating agencies. This report discusses the issue of how to deal with credit rating agencies in a regulatory context within Europe. In particular, the report identifies whether market failures might arise, and, as a result, whether there is a need for the introduction of some sort of recognition and/or regulation of rating agencies as these are generally not regulated in Europe.  In its main conclusions, CESR proposes that on the development of appropriate rules of conduct, CESR advises the European Commission that, overall, the substance agreed by the International Organisation of Securities Commissions (IOSCO) Code published in December 2004 provides the right answer to the issues raised by the Commission’s mandate. It is felt that the IOSCO Code will improve the quality and integrity of the rating process and the transparency of credit rating agencies’ operations and reflects the message received from the responses to the consultation.  Therefore in relation to the aspect of the enforcement of the IOSCO Code and more specifically, in respect to the final question asked by the Commission’s mandate: does CESR consider it appropriate that credit rating agencies should be registered in the EU?, CESR is proposing two possible ways of handling this issue, narrowing down the four alternatives originally considered: A clear majority of CESR members supports a ‘wait and see’ approach, where no recognition system is set up at present, and the effects of the IOSCO Code are given time to work, as IOSCO and its members have committed to monitoring the implementation of the code. Should self regulation fail to deliver, there might be a need for statutory regulation. Overall, this approach was shared by respondents to the consultation. A distinct minority of CESR members advocates an EU voluntary recognition system, along with a subsequent reporting on the compliance with the IOSCO code.  The report itself also analyses a potential set of rules of conduct that might apply to rating agencies and the provisions of the IOSCO code in relation to the aspects studied. In particular, the paper considers the various potential conflicts of interests that might arise as well as the fair presentation and methodologies of rating agencies, staff requirements and the relationship between issuers and credit rating agencies. In addition, an analysis of the use of ratings in private contracts and in European legislation is provided.  Amongst the various potential conflicts of interest which CESR discusses, a number arise in the context of the relationship between issuers and credit rating agencies. For example, ratings agencies are often remunerated by the issuers they rate and sometimes provide the issuer with ancillary services which some might consider could lead to a conflict of interest.  In relation to methodologies, CESR discusses a number of transparency requirements that could be placed on rating agencies. For example, one might wish to require ratings agencies to disclose and explain the key elements underlying the rating and to provide an explanation of the assumptions on which the rating is based and the factors to which the rating of an issuer is most susceptible to change.  A further key aspect of advice is the analysis on how credit rating agencies and issuers might effectively work within the requirements of the Market Abuse Directive, in relation to the handling of confidential and market sensitive information.  Finally, as regards the competitive direction of Credit Rating Agency activity in the EU, CESR is of the opinion that the impact of regulatory requirements is not clear and therefore it cannot conclude that any regulatory requirement would either increase or decrease the entry barriers to the rating industry. Thus, CESR does not recommend the use of regulatory requirements as a measure to reduce or remove entry barriers to the market for credit rating.  Further information is available on the CESR website at: [http//www.cesr-eu.org](http://www.cesr-eu.org/" \t "_new)  **1.18 UK laws on corporate manslaughter**  On 23 March 2005 the UK Home Secretary set out new laws to prosecute companies and organisations whose gross failure at senior management level results in a fatality.  The draft Corporate Manslaughter Bill will update existing laws on corporate killing. The proposed new criminal offence of corporate manslaughter will apply when someone has been killed because the senior management of a corporation has grossly failed to take reasonable care for the safety of employees or others. According to the Home Secretary this deals with the key problem with the current law: the need to show that a single individual at the very top of a company is personally guilty of manslaughter before the company can be prosecuted.  The new offence will mean that courts can look at a wider range of management conduct than at present. It focuses responsibility on the working practices of the organisation, as set by senior managers, rather than limiting investigations to questions of individual gross negligence by company managers.  The new offence will be linked to the standards required under existing health and safety laws. The criminal liability of individual directors will not be affected by the proposals. Corporate manslaughter is an offence committed by organisations rather than individuals and will therefore carry a penalty of an unlimited fine rather than a custodial sentence.  The draft legislation is available on the Home Office website at: [http://www.homeoffice.gov.uk](http://www.homeoffice.gov.uk" \t "_new)  **1.19 CEBS starts consultation on supervisory disclosure**  By the end of next year, any interested party will be able to access relevant information on the implementation and application of harmonised prudential banking rules for all EU Member States in a single location, a common format and a common language.  On 23 March 2005 the Committee of European Banking Supervisors (CEBS) announced it is starting a formal consultation on its guidelines for implementing a common European framework for supervisory disclosure. The consultation is open to all interested parties, including supervised institutions, other market participants and end users of banking services. The consultation period will last for three months. The CEBS guidelines stem from the proposed EU legislation (the Capital Requirements Directive, or CRD) for a new capital adequacy framework for credit institutions and investment firms.  The main purposes of the supervisory disclosure framework are to provide a comprehensive overview of regulatory and supervisory rules in the EU relating to the proposed CRD and to enable meaningful comparison of the approaches adopted by national authorities. It will provide qualitative information, such as regulations and information on the ways in which Member States have exercised the options and national discretions contained in the proposed CRD, as well as quantitative information, such as national statistical data about the banking industry.  CEBS believes that this coordinated move towards grater transparency will contribute significantly to ensuring consistent implementation of the new capital adequacy framework throughout the EU, and enables supervisors to carry out their tasks in an open, accountable but nonetheless independent manner.  The supervisory disclosure framework has been designed to be user-friendly, using the internet as a convenient way to present and make the information easily accessible. The CEBS website ([www.c-ebs.org](http://www.c-ebs.org" \t "_new)) will provide a general overview of the disclosures and will contain links to the websites of the national authorities where more detailed information in the same format will be displayed.  A demonstration of the supervisory disclosure framework is available on the CEBS website at: [http//www.c-ebs.org/SD/SDTF.htm](http://www.c-ebs.org/SD/SDTF.htm" \t "_new)  The supervisory disclosure framework will be modified as necessary to reflect the final version of the CRD, comments received during the consultation, and the results of other CEBS work streams.  The guidelines for implementing the supervisory disclosure framework should be finalised by year-end 2005. The framework will then be implemented by year-end 2006 the target date for qualitative information. Statistical information that institutions use to measure their risks and determine their capital adequacy will be included by mid-2008, recognising that some of the intended content may not yet be available at that time.  More information about the consultation is available on the CEBS website at: [http://www.cebs.org/Consultation\_papers/consultationpapers.htm](http://www.c-ebs.org/Consultation_papers/consultationpapers.htm" \t "_new)  **1.20 Australian financial stability review**  The Reserve Bank of Australia has published its Financial Stability Review. The overview to the Review is provided below.  The Reserve Bank’s overall assessment is that the Australian financial system is in sound condition. Banks - the most important intermediaries from a systemic risk perspective - are well capitalised, highly profitable and experiencing levels of bad debts that are very low by both historical and international experience. Further, there are no signs of the excesses in the commercial property market that were the cause of significant problems for the banking system in the early 1990s. Corporate balance sheets are in very good shape, with interest-servicing burdens around the lowest level for many years. The insurance sector is also performing better than it has for some time, notwithstanding the emergence of competitive pressures in some business lines and claims returning closer to long-term averages.  Given these favourable outcomes, attention has been focused on household balance sheets, which have expanded rapidly. Over 2003, both household debt and house prices increased by around 20 per cent, and this followed large increases in previous years. The Bank’s concern at the time was that a continuation of these trends would increase the likelihood of quite large corrections in house prices and household behaviour at some point in the future. This concern was not so much that these adjustments would imperil the health of financial institutions, but rather that they could lead to a period of weak economic growth.  In the event, 2004 unfolded favourably. Sentiment in the housing market finally turned in late 2003, with house prices falling slightly in some areas over the first three quarters of 2004 before recovering a little. Household credit growth also moderated from the rapid pace of 2003, although it remains quite high relative to the growth of incomes and, hence, servicing capacity.  Despite these welcome developments, the current environment is not without its vulnerabilities. At the global level, low interest rates in the major financial centres, combined with reasonable economic outcomes, have encouraged borrowing and led investors to perceive risk as very low and/or to accept less compensation for holding risky assets. The resulting concern is that in the benign environment of the past few years investors may have underestimated risks and borrowed too much. The corollary of this is that the prices of some assets may have been pushed to unsustainable levels. If this turned out to be the case, developments of recent years could have created the basis of future difficulties.  While the recent benign conditions in financial markets may well continue, if history is any guide, a reappraisal of risk and debt levels is likely at some point in time. Exactly what the trigger for any reappraisal might be is unpredictable. But there are a number of possible candidates. One is an unanticipated rise in inflationary pressure in the global economy, leading to a significant increase in interest rates. Other, but less likely, triggers include a sharp fall in the US dollar due to concerns about the sustainability of the US current account and fiscal deficits, disorderly adjustments in exchange rates in Asia, and a confluence of credit events, including the default or downgrading of a major borrower. A year or so ago, tightening of US monetary policy would have been added to this list, although to date the tightening, if anything, appears to have reinforced the perception that risk is low, rather than the reverse.  Although disruptions in global capital markets arising from an abrupt reappraisal of risk would undoubtedly have effects on Australia, domestically, the main risks continue to revolve around the behaviour of households and their willingness to take on debt, particularly for housing. On one hand, there is the possibility that last year’s favourable developments turn out to be only a temporary reprieve and that the housing market reignites, an outcome that would throw the possibility of a future costly correction back into sharp focus. On the other, there is a risk that the weakening in the housing market could become more pronounced and that households, after taking a more cautious approach to their finances over the past year, may attempt to shore up their balance sheets appreciably. On the basis of how events have evolved to date, both these risks seem to be relatively low, but they cannot be ruled out.  Another uncertainty is the response of Australian financial intermediaries to the slowdown in household credit growth. The concern here is that some intermediaries may be responding to this slowdown by taking on more risk, and at lower margins, in an attempt to preserve lending volumes and market shares. In a number of areas, lending practices are diverging some way from the tried-and-tested methods of the past: far more use is now being made of brokers; ‘low-doc’ lending, which involves a strong element of self-verification in the loan application process, is growing rapidly; and the discounting of home loan rates is much more widespread. To the extent that these various changes are the outcome of a more competitive market they are to be welcomed, provided that lending institutions fully understand the risks involved and are pricing those risks appropriately. Whether or not this is the case will only be evident in a weaker economic environment, when the risk now being built up materialises. While these recent developments do not represent an immediate threat to the financial system, they nonetheless need to be closely watched in the period ahead.  The full Reserve Bank report is available at: [http://www.rba.gov.au/PublicationsAndResearch/FinancialStabilityReview/financial\_stability\_review\_0305.html](http://www.rba.gov.au/PublicationsAndResearch/FinancialStabilityReview/Reviews/financial_stability_review_0305.pdf" \t "_new)  **1.21 Global corruption report**  On 16 March 2005 Transparency International published its Global Corruption Report 2005.  The report focuses on corruption in construction and post-conflict reconstruction. The report includes expert reports on:   * Post-conflict reconstruction, with a detailed analysis of corruption in Iraq; * The mechanisms of corruption in construction projects, from infrastructure development in Lesotho to public services in Germany; * The economic cost of corruption in infrastructure; * The environmental risks of corruption in construction; and * The role of multilateral development banks and export credit agencies in financing corruption.   It also includes:   * Detailed assessments of the state of corruption in 40 countries; * Transparency International’s Minimum Standards for Public Contracting and the Transparency International Integrity Pact; * The Business Principles for Countering Bribery in construction; and * The latest corruption-related research, including studies on the links between corruption and other global issues such as pollution, gender and foreign investment.   The report is available at: [http://www.globalcorruptionreport.org/download.html#download](http://www.globalcorruptionreport.org/download.html" \l "download" \t "_new)  **1.22 Research report: employee share ownership schemes**  The Centre for Corporate Law and Securities Regulation at the University of Melbourne has published a new research report titled "Employee Share Ownership Schemes in Australia: A Survey of Key Issues and Themes". The report is by Jarrod Lenne, Richard Mitchell and Ian Ramsay.  Employee share ownership (ESO) schemes have recently been the subject of public policy interest in Australia. The report surveys key issues and themes surrounding ESO schemes in Australia. It explores the varied policy rationales for these schemes, noting both broad bipartisan support and a generally limited conception of their fundamental purpose. The report also outlines the current state of empirical research on their incidence and effects. It is suggested that available information on ESO schemes is patchy and there is no clear picture of Australian practices. In light of an overview of the present regulation of ESO schemes, the report concludes by highlighting further research questions.  The research report is available at [http://cclsr.law.unimelb.edu.au/research-papers/index.html](http://cclsr.law.unimelb.edu.au/research-papers/index.html" \t "_new) |
| **2. Recent ASIC Developments** |
| **2.1 ASIC further extends interim relief for managed investment scheme constitutions**  The Australian Securities and Investments Commission (ASIC) has extended until 30 June 2005 interim relief permitting fund managers in certain circumstances to provide estimates of the transaction costs, value of scheme property and other expenses in setting the application and redemption price for interests in registered managed investment schemes. The relief was due to expire on 31 March 2005.  ASIC last announced it would extend this relief in December 2004. This short extension will allow time to analyse the responses submitted to ASIC's Consultation Paper 'Proposed relief for constitutions of registered managed investment schemes' and to finalise policy development on this topic.  Section 601GA(1)(a) of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) as modified by Class Order [CO 98/52] Relief from the consideration to acquire constitutional requirement, requires a managed investment scheme constitution to make adequate provision for the consideration to acquire an interest in a scheme with only certain defined exceptions that allow the responsible entity to determine the price.  ASIC considers that if a provision of a scheme's constitution allows the responsible entity discretion to determine any part of the issue price or the price paid to a member upon withdrawal, then the constitution does not comply with section 601GA. ASIC is in the process of considering what relief might be granted from these requirements.  On 21 March 2005, ASIC executed an instrument varying 131 instruments that granted relief from section 601GA to certain schemes, so that interim relief that it has already granted remains effective until 30 June 2005 rather than 31 March 2005.  A copy of the amending instrument [05/257] is available in the ASIC Gazette and available from the ASIC website at: [http://www.asic.gov.au](http://www.asic.gov.au" \t "_new)  **2.2 Changes to financial reporting relief for wholly-owned entities**  The Australian Securities and Investments Commission (ASIC) has released changes to the wholly-owned entities financial reporting relief under Class Order [CO 98/1418] Wholly-owned entities.  Under this class order, certain wholly-owned entities may be relieved from the requirement to prepare and lodge financial reports under Chapter 2M of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default), when they enter into deeds of cross guarantee with their parent entity and meet certain conditions.  The main changes to [CO 98/1418] and related pro forma deeds are:  (a) in relation to the certificate by a legal practitioner that is required to be lodged with new deeds of cross guarantee, and with assumption deeds joining a company to an existing deed of cross guarantee, the opinion concerning proper execution of the deed and whether the deed is binding and enforceable on all parties, can now be made 'after having made such enquiries as were reasonable in the circumstances'; (b) the certificate by a legal practitioner or registered company auditor that is required to be lodged with new deeds of cross guarantee, now caters for the different financial reporting requirements for holding entities that are registered foreign companies; and (c) the class order has been updated for the Australian equivalents of International Financial Reporting Standards, which will apply for financial years commencing on or after 1 January 2005.  Entities entering into new deeds of cross guarantee and assumption deeds will need to be particularly mindful of the changes referred to in (a) and (b), as these changes impact on the wording of both the deeds and the relevant certificates.  For financial years commencing on or after 1 January 2005, the financial information required to be included in the notes to the holding entity's consolidated financial statements in relation to the 'closed group' and parties to the deed of cross guarantee, must comply with relevant requirements of the new accounting standards referred to in (c). As far as possible, these requirements are equivalent to the requirements for financial years commencing before 1 January 2005. However, companies will need to have regard to the changed format requirements for financial statements under the new standards.  The amended class order, pro formas and editorial notes are available from ASIC's Infoline by calling 1300 300 630 or from the ASIC website at: [http://www.asic.gov.au/co](http://www.asic.gov.au/co" \t "_new) |
| **3. Recent ASX Developments** |
| **3.1 Changes to the arrangements for the National Guarantee Fund (NGF)**  The NGF provides compensation to clients of ASX Market Participants and, in limited circumstances, Australian Clearing House (ACH) Participants (dealers) in the circumstances set out in Division 4 of Part 7.5 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and [Regulations](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default).  Until 31 March 2005 the NGF covered both fidelity risks and clearing risks. Following ASX's application under s891A of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default), the Commonwealth Government decided to restructure the clearing support arrangements of the NGF. In essence, this restructure, which occurred on 31 March 2005, involved the NGF making a payment to ACH and the repeal of the NGF clearing claims provisions from the [Corporations Regulations](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default).  As a result of the restructure, the NGF now covers fidelity risks only. Clearing risks are covered by ACH.  The changes resulting from the restructure are as follows.  **(a) Before 31 March 2005**  Prior to the restructure, claims could be made on the NGF for:   * buying/selling client contract guarantee claims where there has been a default by the selling/buyer dealer in delivering securities or paying consideration (Regulations 7.5.24 to 7.5.27). These claims are unaffected by the restructure; * buying/selling dealer contract guarantee claims where there has been a default by the selling/buyer dealer in delivering securities or paying consideration (Regulations 7.5.20 to 7.5.23). These claims provisions have now been repealed; * securities loans guarantees default (Subdivision 4.4 of Part 7.5). These claims provisions have now been repealed; * net obligations default (Subdivision 4.5 of Part 7.5). These provisions enabled ACH or a dealer to make a claim on the NGF for non-fulfilment of a net payment obligation or a net delivery obligation on a settlement day. These claims provisions have now been repealed; * compensation for loss that results if a dealer transfers securities without authority (Subdivision 4.7 of Part 7.5). These claims are unaffected by the restructure; * compensation for loss that results if a dealer wrongly cancels or fails to cancel a certificate of title to securities (Subdivision 4.8 of Part 7.5). These claims are unaffected by the restructure; and * compensation for loss that results if a dealer becomes insolvent and fails to meet its obligations to a person who had previously entrusted property to it (Subdivision 4.9 of Part 7.5). * These claims provisions are unaffected by the restructure except that minor changes have been made to the limits of compensation payable under Regulation 7.5.71. Previously the cap on payments under this Regulation was set at 14% of the minimum amount of the NGF. Prior to 31 March 2005, the minimum amount was $80m with the result that this cap was set at $11.2m.   As a result of the restructure, the minimum amount was reduced to $76m and the percentage under Regulation 7.5.71 was increased to 15%. As a result, from 31 March 2005, the cap has been increased to $11.4m.  The changes to the claims provisions noted above, together with various consequential amendments (including the repeal of various definitions) are set out in the [Corporations Amendment Regulations 2005 (No 2)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=83918" \t "default).  **(b) From 31 March 2005**  Following the restructure, the only claims that can be made on the NGF (apart from transitional claims which are discussed below) are those referred to in items 1, 5, 6, and 7 under (a) above.  **(c) Transitional arrangements**  The repeal of the NGF claims provisions noted in items 2, 3 and 4 under (a) above do not apply to claims under Regulations 7.5.20, 7.5.21, 7.5.22, 7.5.23, 7.5.33, 7.5.40 or 7.5.41 that a claimant was entitled to make before 31 March 2005 (and which was not withdrawn or finally determined before that date) and which is served on Securities Exchanges Guarantee Corporation (SEGC) before 30 September 2005 (transitional claims). In other words, transitional claims can still be made on SEGC in certain circumstances, but only for a limited time.  **3.2 Miscellaneous amendments to the ASIC settlement rules**  A number of amendments were made to the ASTC Settlement Rules on 4 April 2005. The amendments are mainly administrative, consequential and/or miscellaneous in nature.  **3.3 Miscellaneous amendments to the ACH clearing rules**  A number of amendments were made to the ACH Clearing Rules on 12 April 2005. The amendments are mainly administrative, consequential and/or miscellaneous in nature. |
| **4. Recent Takeovers Panel Developments** |
| **4.1 National Foods Limited 01: Panel concludes proceedings**  On 15 April 2005 the Takeovers Panel announced that it has concluded its proceedings in relation to the application by San Miguel Foods Australia Holdings Pty Ltd (San Miguel) for a declaration of unacceptable circumstances made on 7 March 2005.  In light of:   * the undertakings received from Fonterra Foods Pty Ltd (Fonterra Foods) and supplementary disclosure by Fonterra Foods in its fifth supplementary bidder's statement on 4 April 2005; and * the announcement by San Miguel on 6 April 2005 of its increased offer for shares in National Foods, and Fonterra Foods' subsequent announcement on 11 April 2005 that it would close its bid for National Foods and accept San Miguel's offer, the Panel has decided to conclude the proceedings and not to make any declaration of unacceptable circumstances in relation to the proceedings.   **(a) Application**  The application concerned a proposed joint venture (Joint Venture) which Fonterra Foods, Yoplait SAS and Sodima SAS announced on 2 March 2005. The Joint Venture was proposed to be implemented between National Foods and Sodima if Fonterra Foods acquired 100% of the shares in National Foods. The Panel announced its receipt of the application in Media Release TP05/25 on 8 March 2005.  **(b) First part of National Foods 01 decision**  The Panel has previously issued Media Release TP05/32 setting out its decision in relation to the first part of the application i.e. issues relating to Fonterra Foods' initial failure to make adequate disclosure of the terms of the Joint Venture, and its intentions for the fixed assets, employees and businesses of National Foods in light of the Joint Venture. The Panel considered that Fonterra Foods' undertakings and supplementary disclosure meant that unacceptable circumstances no longer existed and required no further action.  **(c) Second part of National Foods 01 decision**  The second part of the proceedings related to the need for Yoplait and Sodima to lodge a substantial shareholding notice following their entry into an agreement in connection with the Joint Venture (Fonterra/Yoplait Deed). Proceedings in relation to this issue were suspended pending the outcome of an application by Yoplait and Sodima for relief from the requirement to attach the Fonterra/Yoplait Deed to a substantial shareholding notice.  In light of the changes in San Miguel's and Fonterra Foods' positions in the contest for National Foods, and the Joint Venture consequently not proceeding, the Panel considers that there would now be no material benefit for the market in National Foods shares, or for National Foods shareholders, from Yoplait and Sodima giving substantial holding notices nor from Yoplait and Sodima attaching a copy of the Fonterra/Yoplait Deed to any substantial holding notice. The Panel has consequently consented to Yoplait and Sodima withdrawing their undertakings to give substantial holding notices in relation to the shares in National Foods, held by Fonterra, in which the Panel found Yoplait and Sodima had voting power by virtue of an association with Fonterra.  Further information is contained in the Panel's media release which is available at: [http://www.takeovers.gov.au/display.asp?ContentID=938](http://www.takeovers.gov.au/display.asp?ContentID=938" \t "_new) |
| **5. Recent Corporation Law Decisions** |
| **5.1 Extension of time provisions to be given a liberal construction**  (By Sabrina Ng and Ainslie Baird, Corrs Chambers Westgarth)  In the matter of Tony Barlow Australia Limited [2005] FCA 363, Federal Court of Australia, Nicholas J, 6 April 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/april/2005fca363.htm](http://cclsr.law.unimelb.edu.au/judgments/states/federal/2005/april/2005fca363.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  The Court found that a liberal construction is to be given to its power to make orders avoiding irregularities under section 1322 of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (the Act) and accordingly made orders to correct the late lodgment of an application for the admission of quotation of securities on the ASX.  **(b) Decision**  Tony Barlow Australia Ltd (the Company) was subject to a Deed of Company Arrangement and its shares were suspended from trading. As part of a recapitalisation plan, it sought to seek re-quotation on the ASX of the existing shares and to issue new shares under a prospectus. The prospectus was lodged by the Company, however the quotation application was not lodged until 27 days later, outside the 7 days required by sections 723(3)(a) and 724(1)(b) of the Act. Notwithstanding that failure, the shares were issued pursuant to the prospectus and the shares were officially quoted on the ASX and were capable of being traded.  After discovery of the error, the Company promptly made an application for extension of the time to lodge the quotation application.  **(c) Decision**  Justice Nicholson held that a liberal construction is to be given to the Court's power to make orders to avoid irregularities under section 1322 and that in the circumstances no substantial injustice had been or was likely to be caused to any person. It was noted that it was not a case of blatant nor deliberate non-compliance. Moreover, Nicholson J found that there was more likely to be a materially adverse impact on the Company, its shareholders and creditors if the order was not granted. The prospectus and the funds raised from the issue of the shares were integrally linked to the Company complying with the Deed of Company Arrangement and the coming out of administration.  Justice Nicholson ordered an extension of time for the Company to lodge an application for the admission of quotation of securities on the ASX and also ordered the validation of the shares issued pursuant to section 245E to complete the correction of the errors.  **5.2 Schemes of arrangement: Inadequate disclosure**  (By Martine Pepperell, Articled Clerk, Clayton Utz)  Capel Finance Ltd [2005] NSWSC 286, New South Wales Supreme Court, Barrett J, 4 April 2005  The full text of this judgment is available at [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/april/2005nswsc286.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/april/2005nswsc286.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  Capel Finance Ltd (CFL) sought an order of the Court under section 411(1) of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (Act) to convene a meeting of its members for consideration of a proposed scheme of arrangement. The proposed scheme involved the selective cancellation of ordinary shares in return for a cash payment or the issue of so-called "redeemable preference shares".  The Court refused to grant the order sought on three key grounds. Firstly, there was inadequate disclosure regarding the source and availability of the necessary cash to pay members for their cancelled shares. Secondly, the Court held that the scheme was improperly proposed because the so-called "redeemable preference shares" were not preference shares at all. Finally, the level of disclosure in relation to the so-called "redeemable preference shares" was also held to be inadequate.  **(b) Facts**  At the time of the proceedings, CFL had approximately 22 million shares on issue and sought to cancel all of these shares except those owned by two members who between them held approximately 7 million shares. In cancelling the members' existing shares, the proposed scheme provided each member with three options for receiving the sum referable to their shares:   * the sum would be applied in paying up new shares in the company (described as "redeemable preference shares") on the basis of one new share for each cancelled share; * the sum would be paid in cash; or * the sum would be applied in a combination of these two ways.   The draft explanatory statement for the proposed scheme attempted to describe the source of funds from which any cash payments to members would be paid. The explanatory statement also detailed the rights (or lack thereof) attaching to the so-called "redeemable preference shares".  **(c) Decision**  The Court refused to grant the order sought.  **(i) The law**  In considering whether to order the convening of a meeting of members under section 411(1) of the Act, the Court will consider a range of factors: Re NRMA Insurance Ltd (No 1) (2000) 156 FLR 349. For instance, a court will consider whether there is adequate disclosure to those who will be affected by the arrangement (Re Dorman Long & Co Ltd [1934] Ch 635 at 665) and, more fundamentally, whether the scheme is in fact properly proposed. In relation to disclosure, the Court will have particular regard to the adequacy of the draft explanatory statement required by section 411(3) of the Act.  **(ii) Inadequate disclosure of CFL's ability to pay the maximum cash outlay**  Barrett J determined that if all members participating in the scheme elected to be paid in cash (ie. not receive any redeemable preference shares), CFL would be required to pay out approximately $1.2 million. His Honour referred to CFL's explanatory statement which merely stated that if the maximum cash outlay became payable it would be funded from the company's "cash resources". His Honour concluded that the explanatory statement needed to be amplified in this area to identify clearly the arrangements that were in place to ensure the availability of the maximum cash requirement. In particular, Barrett J drew an analogy with the level of disclosure required in the context of an off-market takeover bid. Consistent with ASIC's views on this issue, his Honour concluded that CFL's explanatory statement should include the same detailed disclosures regarding the availability and source of funding as required by section 636(l)(f) of the Act e.g. the amount of cash already held by the company, the identity of any others who are to provide cash and details of the funding arrangements with those persons.  **(iii) The shares were not "redeemable preference shares"**  Barrett J also found that a share issued on the terms proposed by CFL would not be a redeemable preference share at all. His Honour stated that preference shares can only exist "by way of juxtaposition with other shares" and by having some priority over ordinary shares. Barrett J also noted that holders of preference shares are usually "entitled to some comparative advantage, commonly with respect to one or more of the matters referred to in section 254A(2)", ie: repayment of capital, participation in surplus assets and profits, cumulative and non-cumulative dividends, voting and priority of payment of capital and dividends in relation to other shares or classes of preference shares. Barrett J considered the terms of issue of the proposed scheme with respect to these matters and observed that the so-called "redeemable preference shares" had no priority in relation to any of these matters. In fact, the terms of issue conferred no voting rights whatsoever.  Barrett J found that any shares issued on these terms would carry no priority and therefore could not be described as "preference shares". Whilst the right of a shareholder to require redemption made the shares redeemable, that right did not of itself characterise the shares as "preference" shares. As a result, his Honour concluded that the shares, not being preference shares, could only be redeemed under the capital reduction provisions or the share buy back provisions of the Act rather than Part 2H.2 of Chapter 2H of the Act.  **(iv) Inadequate disclosure of CFL's ability to redeem**  Even though Barrett J concluded that the so-called "redeemable preference shares" would not be "preference" shares, he nevertheless proceeded to consider the redeemability of these shares. In doing so, he referred to section 254K(b) which, notwithstanding that a redemption might be at a shareholder's option, nevertheless precludes a company from redeeming preference shares except out of profits or the proceeds of a new issue of shares made for the purpose of redemption.  In its explanatory statement, CFL acknowledged the risk of there being no available profits to redeem a member's shares. However, Justice Barrett held that this did not go far enough to enable members to obtain an informed understanding of the implications and risks of the scheme. His Honour was critical of the fact that the company still invited members to take the supposed redeemable preference shares in place of their ordinary shares, even though CFL's uncertain financial standing meant that the option to redeem was virtually worthless. In this regard, CFL had ceased to carry on business, had no plans to commence any new business and CFL's balance sheet as at 30 June 2004 showed accumulated losses of more that $48 million. His Honour concluded that the "prospects of profits being available to cover the redemption of redeemable preference shares in the foreseeable future must therefore be regarded as highly problematic."  Barrett J held that there was inadequate disclosure of these redemption difficulties and that CFL's explanatory statement needed to be expanded to fully explain the risks and uncertainties attaching to this aspect of the scheme. Barrett J's conclusion is consistent with ASIC's Policy Statement 142: "Schemes of Arrangement and ASIC Review" which requires that an explanatory statement should include a "clear, prominent statement of, and comparisons of, the advantages and disadvantages of proceeding with or rejecting the scheme." [PS 142.41] Obviously, the unlikely prospect of redemption, when coupled with the lack of any other rights attaching to the preference shares, was a significant disadvantage vis-à-vis the current position of the members as holders of ordinary shares.  **5.3 Are directors parties to a directors and officers insurance contract?**  (By Jane O'Connor, Freehills)  Martin John Green in his Capacity as Liquidator of Arimco Mining Pty Limited (in liquidation) v CGU Insurance Limited [2005] NSWSC 254, New South Wales Supreme Court, Bergin J, 31 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc254.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc254.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  The plaintiff, Mr Green, in his capacity as liquidator of Arimco Mining Pty Ltd (Arimco), made an application pursuant to section 6(4) of the [Law Reform (Miscellaneous Provisions) Act 1946](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=4049" \t "default) (the Act) for leave to proceed against CGU Insurance Limited (CGU) in its capacity as the insurer of the third to sixth defendants, who were the remaining directors of Arimco. CGU is also the first defendant in its capacity as the insurer of the late Phillip Arthur Pearce, a former director of Arimco. Mr Green sought an order under section 588M of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) that the defendants pay the liquidator $25.6m as compensation for loss resulting from alleged insolvent trading.  Together with the application for leave to proceed, the questions for determination by the court were, whether directors are a "party to" the insurance contract, and whether there was a viable defendant.  **(b) Facts**  Arimco was a wholly owned subsidiary of Australian Resources Limited (ARL) which engaged in gold and copper mining. ARL and Arimco had common directors and together with a number of dormant subsidiaries, were managed as a single entity. CGU under the director's insurance policy, had agreed to pay on behalf of the directors any loss for which the directors and officers may not be indemnified by ARL, in this case, the claims made against them in these proceedings.  It was alleged that between 1 January 1999 and 14 March 1999, Arimco traded and incurred debts while insolvent within the meaning of section 59A of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and that the directors were aware that Arimco was insolvent. Mr Green was appointed voluntary administrator of Arimco on 14 March 1999 and liquidator on 14 November 2004 when the Court made orders for the company's winding up. There was also an alternative claim that a reasonable person in the position of the directors would have been aware of the insolvency and as a result, each of the directors had breached section 588G of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default), therefore the liquidator is entitled to recover the $25.6m debt from them under section 588M. CGU, however, argued that leave should not be granted because the directors are not parties to the contract of insurance, but named beneficiaries, whose liability is insured under the contract of insurance.  The questions for consideration on the issues raised by the parties were whether the directors are parties to the contract of insurance and, if they are, whether leave should be refused on the ground that the plaintiff failed to prove that the defendants are not viable defendants.  **(c) Decision**  **(i) Application for leave to proceed**  Section 6 of the Act provides that no action shall be commenced against an insurer on a contract of insurance where the person is indemnified against any liability to pay any damages, except with the leave of the Court. It further states that leave shall not be granted in any case where the Court is satisfied that the insurer is entitled under the terms of the contract of insurance to disclaim liability, and that any proceedings, including arbitration proceedings, necessary to establish that the insurer is entitled to disclaim, have been taken. CGU argued that leave should not be granted because the directors were neither "insured", nor persons who have "entered into a contract of insurance".  In determining whether or not the Court's discretion to grant leave should be exercised, Bergin J articulated what the predominant considerations should be, first, whether Mr Green had shown an arguable case against CGU, and secondly, whether there were sufficient reasons for Mr Green to bring an action against CGU. Further, Bergin J agreed with the view expressed by Young J in Schipp v Cameron (1995) 8 ANZ Insurance Cases 61-256, that "ordinarily, where the plaintiff shows that her case is arguable, then, if there is no other factor involved, leave will be granted". In this context and given the relative modesty of the hurdle, Bergin J granted leave to proceed against CGU as the insurer of the director/defendants dated from 14 December 2004 when the conditional leave was granted.  **(ii) Whether directors party to contract**  This question was similarly considered in CE Heath Casualty & General Insurance Ltd v Grey (1993) 32 NSWLR 25, where Mahoney JA (on appeal) stated the following matters were of significance to support the finding that the directors were parties to the contract of insurance:   * the extent of the directors' knowledge that insurance was being effected for their benefit; * the extent of the directors' involvement in carrying out the arrangements under the package proposal; * the commercial context of the insurance package; and * the obligations under the policy.   In the present case, Bergin J similarly considered that the evidence established the directors had knowledge that the insurance was being effected and was for their benefit.  The Judge also failed to accept CGU's suggestion that the Declaration signed in the proposal form by the directors demonstrated they were not part of the insurance contract. She argued that the commercial context, and the context generally, supported her finding that the directors were in fact parties to the insurance contract and that this was evidenced by the policy document stating that the Insurer would provide the indemnities set out in the policy in consideration of the payment of the premiums. Her Honour also found that the commercial context of the directors and officers being under Insuring Agreement A and the Corporation being insured under Agreement B, meant that the Directors were specifically intended to be parties to the contract of insurance.  The use of two separate Agreements, she argued, meant that it was not merely the company that was supposed to be a party to the contract. Her Honour therefore held that the defendant directors were parties to the contract of insurance within the meaning of section 6 of the Act.  **(iii) Whether viable defendant**  After considering evidence in relation to the financial circumstances of the defendants and their capacity to satisfy a judgment of $25.6 million, her Honour was satisfied that the plaintiff had proven that it was more probable than not that there was no viable defendant.  **5.4 Provision in constitution of company whereby a member ceases to be a member if he becomes bankrupt**  (By Chris Skordas, Phillips Fox)  Battenberg v Union Club [2005] NSWSC 242, Supreme Court of New South Wales Equity Division, Campbell J, 30 March 2005  The full text of this judgement is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc242.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc242.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  An application was brought by Lord Andrew Charles Robert Battenberg (plaintiff) seeking, among other things, a declaration that the Union Club (defendant) was not entitled to rely upon a sequestration order to deny him membership of the Union Club. The Articles of Association of the defendant included a provision stating that a member shall cease to be a member if he becomes a bankrupt. The plaintiff became bankrupt, however the defendant did not become aware of the bankruptcy until after the bankruptcy had been annulled. The defendant attempted to rely upon its Articles of Association to deny that the plaintiff had been a member since he became bankrupt.  His Honour Justice Campbell, in entering judgement for the plaintiff, concluded that in this circumstance the effect of the annulment was that the bankruptcy never existed, and therefore the plaintiff had always been, and remained, a member of the defendant.  **(b) Facts**  **(i) Background**  The defendant was a corporation limited by guarantee. Clause 16(b) of the company's Articles of Association provided: 'A member shall cease to be a member if he becomes bankrupt or enters into a deed of assignment, a composition or a scheme of arrangement with his creditors under Part X of the [Bankruptcy Act 1966](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default) (as amended).'  On 6 October 1992 the plaintiff became a member of the defendant. On 19 May 1997 the Federal Court of Australia made a sequestration order against the estate of the plaintiff, pursuant to section 43(1) of the [Bankruptcy Act 1966](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default). Section 43(2) of the [Bankruptcy Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default) provides that:  'Upon the making of a sequestration order against the estate of a debtor, the debtor becomes a bankrupt, and continues to be a bankrupt until:   * he or she is discharged by force of subsection 149(1) or in accordance with Division 3 of Part VII; or * his or her bankruptcy is annulled by force of subsection 74(5) or 153A(1) or under section 153B'.   On 23 March 2000 the plaintiff's bankruptcy was annulled by a special resolution of a meeting of creditors, pursuant to section 74(5) of the [Bankruptcy Act 1966 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default).  The defendant first becomes aware of the sequestration order on or around April 2001.  After correspondence between the plaintiff's solicitor and the defendant, the defendant wrote to the plaintiff on 16 August 2001 informing him that pursuant to clause 16(b) he had ceased to be a member on 19 May 1997.  At all times between 19 May 1997 and 16 August 2001 the defendant accorded the plaintiff with the usual and full rights of a member and the plaintiff made membership payments to the defendant.  **(ii) Submission of the plaintiff and orders sought**  The plaintiff submitted that, subject to the exceptions in the [Bankruptcy Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default) and certain common law exceptions not relevant to the facts, an annulment of bankruptcy requires that the bankruptcy be treated as having never occurred.  The following orders were sought by the plaintiff:   * A declaration that on the true construction of clause 16(b) of the Articles of Association of the defendant, and in the events surrounding the case, he did not cease to be a member of the defendant by reason of the sequestration order; * A declaration that the defendant was not entitled on or about 16 August 2001 or at any time thereafter to rely upon the sequestration order to deny him membership; * A declaration that he was at all material times and is a member of the defendant; * An injunction restraining the defendant from asserting that the plaintiff is not a member of the defendant by reason of the sequestration order and prior bankruptcy; and * An order that the defendant pay to the plaintiff damages the plaintiff has sustained by reason of it not recognising him as a member.   **(iii) Submission of the defendant**  The defendant submitted that the task before the court was fundamentally one of construction of clause 16(b) of the Articles of Association. Further, the defendant submitted that clause 16(b) was a self-executing provision that operated automatically as soon as bankruptcy occurred. Finally, the defendant submitted that if the operation of clause 16(b) were reversed on annulment of bankruptcy, there would be an inconsistency between the treatment of bankrupts under the clause and the treatment of members who enter into arrangement with their creditors under Part X of the [Bankruptcy Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default).  **(c) Decision**  His Honour commented that the task before the court was not simply one of construction of clause 16(b), but also of deciding how it operates. His Honour also confirmed that a rule whereby someone ceases to be a member upon bankruptcy is self-executing; however his Honour held that the real question to be decided was whether, in light of the annulment, it was now open to the Court to decide that the plaintiff was someone who had ever become bankrupt.  His Honour considered the range of consequences triggered by bankruptcy, including disqualification from managing corporations if a person is an undischarged bankrupt, pursuant to the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default).  His Honour then considered the effect of annulment in other areas of the law, including judgments whereby:   * the setting aside of a criminal conviction involved it being held to be, retrospectively, of no effect; * a declaration of nullity of marriage was held to have a retrospective effect; and * the subsequent reversal of a decision to dismiss an employee pursuant to a statutory power entitled the employee to wages for the period between the initial dismissal and its reversal.   However, his Honour noted that a judgment which is consequently set aside will not always be of no effect. In particular he set out the following exceptions:   * whether what has been done can be undone, given the availability of appropriate remedies (for example, where statute allows an entry in a register to be rectified, but not removed); * where there has been an act of bankruptcy arising from a failure to comply with a bankruptcy notice; * in some circumstances, where a judgment has been acted upon before it is overturned on appeal; and * where giving effect to another statute requires that the annulment not be in all respects retrospective.   His Honour concluded that although treating an act in law as having a retrospective effect has considerable artificiality, that sort of artificiality is inherent in the notion of an event being "annulled". Therefore, subject to the exceptions which the [Bankruptcy Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default) creates, and exceptions which arise as a matter of general law, a bankruptcy which is annulled is treated as not having occurred. Accordingly, given that none of the exceptions outlined by Campbell J were relevant to the facts of this case; his Honour held that the plaintiff was entitled to the declarations and injunction sought. The plaintiff did not adduce evidence regarding the issue of damages, and therefore none were awarded.  His Honour acknowledged the inconsistency between the treatment of bankrupts under Clause 16(b) and the treatment of members who enter into deeds of arrangements with their creditors under Part X of the [Bankruptcy Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6559" \t "default). However he concluded that the inconsistency was not a reason for rejecting what would otherwise be the effect of a statute.  **5.5 Interpretation of the civil penalty provisions of the Corporations Act**  (Taryn Gollasch, Mallesons Stephen Jaques)  One.Tel Limited (In Liquidation) v John David Rich [2005] NSWSC 226, New South Wales Supreme Court, Bergin J, 23 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc226.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc226.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  Only ASIC has standing to seek declarations of contravention of the civil penalty provisions listed in section 1317E of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and the [Corporations Law](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=7375" \t "default).  Proceedings brought by a corporation for an order of compensation under sections 1317H or 1317HA of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (and their predecessors in the [Corporations Law](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=7375" \t "default)) are not proceedings for the imposition of a penalty.  The Notes in sections 1317E, 1317H, 1317HA and 1317J(2) are part of the text of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) and do not fall within the concept of marginal note, endnote or footnote in the [Acts Interpretation Act 1901](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6818" \t "default).  Defendants in proceedings brought by a corporation for an order of compensation under sections 1317H or 1317HA of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (and their predecessors in the [Corporations Law](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=7375" \t "default)) for contravention of the civil penalty provisions are not obliged to submit evidence in such proceedings as it may be used to establish their liability to a penalty in later proceedings brought by ASIC for contravention of the civil penalty provisions.  **(b) Facts**  The plaintiff, One.Tel Limited (In Liquidation), filed an amended summons on 3 November 2004 (Amended Summons) seeking against John David Rich (Rich) and Rodney Stephen Adler (Adler) (and other directors of the plaintiff) declarations of contravention of certain civil penalty provisions of the [Corporations Act 2001](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (the Act) and the [Corporations Law](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=7375" \t "default) (the Law). During the hearing, the plaintiff indicated that it would no longer press for any declarations of contravention of civil penalty provisions and would only seek, pursuant to section 1317J(2), an order for compensation under section 1317H of Part 9.4B of the Act and/or its predecessor under the Law, section 1317HD of Part 9.4B.  In response, the defendants, Rich and Lifecell Pty Ltd (Lifecell), sought by Notice of Motion (the Rich/Lifecell Motion) an order that:  (i) the Amended Summons be summarily dismissed or struck out; (ii) further and alternatively, a declaration that the proceedings are a proceeding for the imposition of a penalty; and (iii) further that the order made for Rich and Lifecell to file and serve evidence be vacated.  The defendant, Adler, sought by Notice of Motion (the Adler Motion) the same relief as sought in items (i) and (ii) of the Rich/Lifecell Motion.  **(c) Decision**  **(i) Corporations have no standing to apply for declarations of contravention of civil penalty provisions**  Bergin J stated that the defendants' request for summary dismissal of the Amended Summons was obviated by the plaintiff's indication that it would no longer press the claims for declarations of contravention under section 1317E. Her Honour also stated, however, that it was clear that the plaintiff had no standing to seek such declarations. Under section 1317J of the Act, ASIC is permitted to apply for such declarations, but corporations are limited to applying for compensation orders. Section 1317J(4) states that unless permitted by section 1317J, no person may apply for such declarations.  **(ii) Proceedings for compensation are not proceedings for the imposition of a penalty**  Bergin J refused the applications for a declaration that the proceedings were for the imposition of a penalty.  The defendants sought such a declaration with the aim of preventing the plaintiff from tendering in chief extracts from the examinations of various former officers of the plaintiff, including Mr Rich. The defendants' argument was that if the Court is satisfied that the defendants have contravened a civil penalty provision in these proceedings, it "must" make a declaration of contravention in accordance with section 1317E of the Act and/or section 1317EA of the Law. This would then expose the defendants to the seeking by ASIC of a pecuniary penalty order or a disqualification order. (The Note to section 1317E makes it clear that ASIC is entitled to seek a pecuniary penalty order or a disqualification order once a declaration of contravention is made). Bergin J rejected such argument.  Instead her Honour accepted the plaintiff's submission that the obligation of the Court to make a declaration of contravention under sections 1317E and 1317EA only applies to proceedings in which ASIC seeks a declaration of contravention and a pecuniary penalty pursuant to section 1317J(1) of the Act or section 1317EA(3) of the Law, and does not apply where compensation is sought by a corporation under section 1317H or section 1317HA of the Act, as it was in this case.  Her Honour reasoned that reading the Note in section 1317E together with sections 1317J and 1317H(1)(a) makes it clear that section 1317E only applies to applications brought by ASIC, which is a gateway to other relief that it may seek, being the pecuniary penalty order and/or the disqualification order, and that it is not a gateway to an order for compensation under section 1317H or 1317HA. She also stated that interpreting section 1317E to require a court to make a declaration when it is satisfied of a contravention of civil penalty provisions in an application by a corporation under section 1317J(2) for a compensation order, would make nonsense of the Notes in sections 1317H and 1317HA.  **(iii) Status of statutory notes**  In coming to the above conclusion, Bergin J found that the Notes to sections 1317E, 1317H, 1317HA and 1317J(2) form part of the text of the Act and do not fall within the concept of marginal note, endnote or footnote in the [Acts Interpretation Act 1901](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=6818" \t "default). The basis for this finding is as follows. First, the Notes to sections 1317J, 1317H and 1317HA are the subject of an express provision in the [Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=78496" \t "default) (the 2004 Act) that the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) is "amended or repealed" as set out in the relevant schedule of the 2004 Act. Second, the Explanatory Memoranda (EM) to the 2004 Bill expressly refers to the Notes in sections 1317J, 1317H and 1317HA as "amendments".  **(iv) Privilege available in penalty proceedings applies in proceedings for compensation for contravention of civil penalty provisions**  Bergin J vacated the order requiring the defendants to file evidence in the proceedings. Her Honour said that it was a matter for them whether, at the end of the plaintiff's case, they intend to call evidence to defend the proceedings.  Her reasoning was that such an order offends the principle expounded by Deane J in Refrigerated Express Lines (A/Asia) Pty Ltd v Australian Meat and Live-Stock Corporation [1979] 42 FLR 204, at 207-208, that a party to litigation ought not to be compelled to provide information or produce documents for inspection by the other party if the result will be to provide evidence against him which may be used to establish his liability to a penalty in other proceedings. Such principle is applicable in this case because if the defendants in these proceedings were required to furnish information in relation to the application for compensation for contravention of the civil penalty provisions, ASIC could use such information as proof in a later action for a declaration under section 1317E with consequential orders for disqualification and/or pecuniary penalties. Applying the principle in these proceedings will prevent a circumvention by ASIC of the privilege available to the defendants in penalty proceedings.  **5.6 Shareholder cannot sue for loss that is merely reflective of loss suffered by company**  (By Chelsea Spagnolo, Mallesons Stephen Jaques)  Thomas v D'Arcy [2005] QCA 68, Supreme Court of Queensland (Court of Appeal), McPherson and Williams JJA and White J, 18 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/qld/2005/march/2005qca68.htm](http://cclsr.law.unimelb.edu.au/judgments/states/qld/2005/march/2005qca68.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  This case is authority for the proposition that in circumstances where separate duties are owed both to a company and to a shareholder in that company, the shareholder cannot recover damages that are merely reflective of losses sustained by the company.  **(b) Facts**  Graham Thomas (the Plaintiff) owned:   * 50% of all issued shares in Movado Pty Ltd (Movado); * 50% of all issued shares Meadowbury Pty Ltd (Meadowbury); and * certain residential property known as "Moon Lane" (Moon Lane).   Movado owned:   * 100% of the all issued shares in Carphone Company of Great Britain Pty Ltd (Carphone); and * certain land known as "Dunshane" (Dunshane).   D'Arcy and the other defendants were members of a firm of solicitors (the Defendants) which in 1987 agreed to provide legal services to the Plaintiff and to Carphone.  In 1989 and 1990, the National Australia Bank (the Bank) provided loans to Movado, Meadowbury and Carphone. The loans were secured by:   * charges over the assets of each of the companies; * registered mortgages over Moon Lane and Dunshane; and * guarantees from the Plaintiff and his wife.   The effect of section 88 of the [Property Law Act 1974 (Qld)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=12558" \t "default) is that, if the securities were realised, the Plaintiff was entitled to retain any surplus remaining from his:   * shareholding in Movado; * shareholding in Meadowbury; and * interest in Moon Lane.   In 1990, the Bank proceeded to realise the secured assets. Moon Lane and Dunshane were sold by the Bank in 1991.  The Plaintiff claimed:   * the Bank's agent, in disposing of the assets, acted in wilful or reckless disregard of the Plaintiff's interests and in breach of the statutory duty to take reasonable care to ensure that the secured assets were sold at market value; * the Defendants breached their retainer or were negligent by failing to advise the Plaintiff of steps he could have taken to restrain the Bank and its agent from acting the way it did; and * but for that failure by the Defendants, the Plaintiff could have retained Moon Lane and all or a part of the value of his shareholdings in Movado and Meadowbury.   The Plaintiff commenced an action for damages representing all or part of the value of his shareholdings in Movado and Meadowbury and/or the Moon Lane property.  At first instance, Douglas J made an order striking out that part of the Plaintiff's claim for damages relating to his shareholding in the two companies on the basis that a shareholder of a company is not entitled to claim or recover damages for loss measured by a diminution in the value of shares that results from loss or injury to the assets of the company.  The Plaintiff appealed to the Court of Appeal of the Supreme Court of Queensland.  **(c) Decision**  The appeal was unanimously dismissed. Williams JA and White J agreed with McPherson JA's judgment.  **(i) Legal principles**  McPherson JA considered three circumstances that may give rise to a diminution in the value of shares in a company. These circumstances are:   * when an actionable wrong is committed against a company alone; * when an actionable wrong is committed against a shareholder alone; and * when actionable wrongs are committed against both a shareholder and the company.   **(ii) Category 1**  Where a company suffers loss (i.e. a loss or depletion of corporate assets) and the cause of action is vested in the company, the company alone can sue. In these circumstances, the shareholder does not suffer any personal loss. The shareholder's loss is through the company in the diminution in the value of his or her shareholding. As the shares themselves are not directly affected by any wrongdoing, the company itself is the only proper plaintiff.  This outcome is a direct consequence of the well established principles that a corporation is a distinct entity from the shareholders who comprise it and that, accordingly, a shareholder has no proprietary interest in the assets of the company.  A shareholder may sue 'derivatively' for some wrongs. However, in these instances the shareholder is bringing proceedings on behalf of the company and in the company's name. Any relief will belong to the company and not to the shareholder personally.  **(iii) Category 2**  A shareholder can sue and recover for a diminution in the value of his or her shareholding if the diminution occurs as a result of a legal wrong done to him or her personally and if the company has no cause of action in respect of the same loss. In these circumstances, the company's assets will not be depleted by recovery of damages by the shareholder.  **(iv) Category 3**  Where the company suffers loss caused by a breach of duty owed both to the company and the shareholder, the shareholder's loss (in so far as it is measured by the diminution in the value of his or her shareholding) merely reflects the loss suffered by the company. In such cases, the shareholder is not allowed to claim or recover such loss. If the shareholder were allowed to recover loss in these circumstances, there would either be double recovery at the expense of the defendant, or the shareholder alone would recover at the expense of the company, its creditors and other shareholders.  **(v) Application of legal principles to Plaintiff's shareholdings in Movado and Meadowbury**  McPherson JA concluded that the Plaintiff's claim with respect to his shareholding in Movado and Meadowbury was really an attempt to recover a loss suffered by those companies and that it was not sustainable.  The breaches of duty relied upon by the Plaintiff were the Defendants' negligence and their breach of retainer. However, the measure of the loss the Plaintiff sought to recover from the Defendants was the diminution in the value of his shares in Movado and Meadowbury. Such loss was merely a reflection of the loss sustained by those companies as a result of the mortgagee's (i.e. the Bank's) sale of land below market value. That is, the Plaintiff, as a shareholder, was trying to recover loss measured by the diminution in value of his shareholding in a category three situation. The Plaintiff's claim was not sustainable and the appeal was dismissed.  **5.7 Entry into loan facility not an unconscionable transaction**  (By Michelle Burton, Phillips Fox)  Crowe v Commonwealth Bank of Australia [2005] NSWCA 41, New South Wales Court of Appeal, Sheller JA Tobias, JA Bryson and JA, 14 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc41.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc41.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  The Appellant (Mrs Crowe) executed a mortgage over a residential property (the mortgage) in favour of the respondent (the Bank). The mortgage secured certain loan facilities made by the Bank in 1994 and 2000 for her husband's farming business. The borrower defaulted under these facilities and the Bank instituted proceedings against Mrs Crowe, claiming possession of the property as a precursor to its sale.  Mrs Crowe sought to resist the Bank's claims by reliance on the principles stated in Commercial Bank of Australia Ltd v Amadio (1983) 151 CLR 447 relating to unconscionable transactions and also under the provisions of the [Contracts Review Act 1980 (NSW)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=10771" \t "default). Mrs Crowe claimed that the 1994 loan facility was improvident, and because of her lack of education and business experience, she was unable to judge for herself whether the transaction was improvident, whereas the Bank knew that it was unlikely that the loan facility could be serviced in the short term. Mrs Crowe claimed that this imbalance of bargaining power meant that she was at a special disadvantage or disability in the Amadio sense, and it was therefore incumbent on the Bank to ensure that Mrs Crowe received independent financial advice before entering into the transaction. Failure to do so rendered entry into the transaction unconscionable.  In a joint judgement, their Honours Justices Tobias, Sheller and Bryson of the Supreme Court of New South Wales dismissed the appeal, affirming the trial judge's decision that although it would involve some trading loss in the first year, the 1994 loan was a provident transaction which was worthy of the Bank's support. Further, Mrs Crowe understood the nature and effect of the mortgage, she was not in a position of special disadvantage in relation to the Bank, and even if she had obtained independent financial advice she would have proceeded with the transaction.  **(b) Facts**  The 1994 transaction came about as follows. In 1993 Mrs Crowe granted a mortgage over her property to enable Darkcm Pty Limited (Darkcm) to borrow funds to commence a farming operation involving the leasing of three rice farms and the purchase of a breeding pair of ostriches. Mr and Mrs Crowe were the sole directors and shareholders of Darkcm.  In 1994, the Crowes' accountant, Anderson, prepared a funding proposal for Darkcm to borrow from the Bank. The proposal asserted that Mr Crowe had extensive experience in rice farming, having worked in the area all his life and been heavily involved in the operation of his parents' property for many years. Annexed to the proposal was a cashflow for the first three years of the proposed venture also prepared by Anderson.  The Bank's valuer, Connolly, produced a report which noted that Mr Crowe was capable of undertaking a large farming operation, however his financial control and management would need to be improved. Connolly observed that the cashflows contained in his report varied significantly to those submitted by Anderson. Connolly's cashflow excluded the ostrich-breeding venture, as it would only aggravate what was a shortfall of working capital for the first 12 months of the operation. He noted that the revised cashflow should be discussed with the customers to ensure that they were aware of the situation and their need to generate further income, or to obtain other sources of working capital.  The revised cashflow was discussed with Mr and Mrs Crowe, who further advised that they were arranging Rice Board orders which, if approved (and they were confident they would be), would defer payment of major sowing expenses until the first pool payment in May 1995 in respect of the rice crop.  The Crowes requested that the relevant bank documents be forwarded to their solicitor for an "independent explanation of documents and to witness customers execute same". The evidence of the Crowes' solicitor was that he had advised Mrs Crowe that she could lose her house if Darkcm did not repay to the Bank the monies which were to be advanced under the 1994 loan facility.  The Bank conducted a "post-approval review" by its Credit Administrator, who noted that the customers could not service the facility in the short term, and stated: "I do not believe this is a loan that should have been approved. Two other officers within Business Credit have reviewed the file and agree with me… We are now committed to a higher level of risk than the Bank would normally seek."  **(c) Decision**  Their Honours Justices Sheller, Tobias and Bryson upheld the findings of the trial judge and dismissed the appeal.  **(i) Amadio unconscionability**  In Amadio it was established that relief on the ground of unconscionable conduct will be granted when unconscientious advantage is taken of an innocent party whose will is overborne so that it is not independent and voluntary. Justice Tobias articulated the reasoning for finding that Mrs Crowe had not made out such an argument as follows:  Mrs Crowe understood the general nature and effect of the mortgage. She knew that if she borrowed money from a Bank she was liable to repay it, and she understood that if she gave the mortgage over the property to the Bank there was a risk of losing it if the borrower defaulted. His Honour held that she was prepared to take that risk because she trusted her husband's assurances that the payments under the loan facility would be made or, if they were not, the Bank would recover the full amount owing to it by enforcing a bill of sale over certain plant and equipment.  What may have been an improvident transaction as originally proposed was rendered provident when the ostrich breeding venture was deleted from it and when allowance was made for the extra funds which were to be generated from Rice Board orders and the other sources of income. It was the Bank's genuine and reasonable view that Darkcm would generate sufficient income to service and reduce the debt within the period of the proposed rice farm leases as a consequence whereof the venture was worthy of the Bank's support. It was therefore untrue that the Bank knew or ought to have known that it was likely that Darkcm would be unable to service repayments whether in the short or the long term.  Further, his Honour noted that Mrs Crowe was not (unlike Mr and Mrs Amadio) a third party guarantor having no interest in, nor entitled to receive any benefit from, the transaction that she guaranteed. She was both a director and equal shareholder with her husband in Darkcm, which was the borrower. The joint and several guarantees, which the Bank required her and Mr Crowe to execute, was a guarantee by the directors of the borrower company. As such, she and Mr Crowe were, in truth, the real borrowers.  There was therefore no relevant inequality in the bargaining position of Mrs Crowe on the one hand, and the Bank on the other, in terms of her ability to appreciate the risks involved in the transaction and to protect her own interests with respect thereto.  Following this, it was not incumbent upon the Bank's officers to recommend that Mrs Crowe receive independent financial advice. Even if such advice had been recommended, there was no evidence to support Mrs Crowe's submission that if she had received financial advice with respect to the transaction, she would have regarded it as too risky and would have declined to proceed with it.  **(ii) The Contracts Review Act 1980**  In relation to Mrs Crowe's claim based on the [Contracts Review Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=10771" \t "default), his Honour Justice Tobias noted that the critical consideration was whether there was any material inequality in bargaining power between Mrs Crowe and the Bank. His Honour held that it followed from the findings on the Amadio issue that there was no relevant inequality in the bargaining position of Mrs Crowe on the one hand, and the Bank on the other, in terms of her ability to appreciate the risks involved in the transaction and to protect her own interests with respect thereto. Accordingly, Mrs Crowe's claim under the [Contracts Review Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=10771" \t "default) was also rejected.  **5.8 Application for termination of winding-up order under section 482**  (By Kylie Lane, Blake Dawson Waldron)  Metledge v Bambakit Pty Ltd; Manuel Koutsourais, Applicant [2005] NSWSC 160, New South Wales Supreme Court, Barrett J, 11 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc160.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc160.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  In discussing an application to terminate a winding up order under section 482 of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) ("Corporations Act"), Barrett J confirmed the "useful guidance" of the criteria set out in Re Warbler Pty Ltd (1982) 6 ACLR 526. Proof of solvency of the company appears critical to the success of an application; the onus of proof being on the Applicant. Discussing the factors to be considered in determining whether or not the conduct of the company was contrary to "commercial morality", Barrett J noted that actions following the making of the winding up order, the attitude of the director, evidence of continuing "sloppy" commercial behaviour, and the state of the company's books of record and account were relevant in denying the application.  **(b) Facts**  Mr Manuel Koutsourais is sole director and one of two shareholders in Bambakit Pty Ltd ("Bambakit"). The other shareholder is an accountant, Mr Kristallis, who holds the shares on trust for members of Mr Koutsourais' family. An order was made that Bambakit be wound up in insolvency following failure to pay a judgment debt. The applicant for the winding up was Ms Metledge, a solicitor. The debt was for sums alleged to be owed to her for legal services. Mr Koutsourais made an application under section 482 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) for an order terminating the winding up of Bambakit.  Section 482 confers a discretionary power on the court to "make an order staying the winding up indefinitely or for a limited time or terminating the winding up." Barrett J referred to the criteria set out by Master Lee QC in Re Warbler Pty Ltd (1982) 6 ACLR 526 as providing useful guidance to the exercise of the discretion:   * the granting of a stay is a discretionary matter, and there is a clear onus on the applicant to make out a positive case for a stay; * there must be service and proof of notice of the application for a stay on all creditors and contributories; * the nature and extent of the creditors must be shown, and whether or not all debts have been or will be discharged; * the attitude of creditors, contributories and the liquidator is a relevant consideration; * the current trading position and general solvency of the company should be demonstrated (solvency is of significance when a stay of proceedings in the winding-up is sought); * if there has been non-compliance by directors with their statutory duties as to the giving of information or furnishing a statement of affairs, a full explanation of the reasons and circumstances should be given; * the general background and circumstances which led to the winding-up order should be explained; and * the nature of the business carried on by the company should be demonstrated, and whether or not the conduct of the company was in any way contrary to "commercial morality" or the "public interest".   ASIC had successfully prosecuted Mr Koutsourais under section 530A of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) for failing to comply with his obligations to provide a report as to affairs of the company and deliver books and records to the liquidators.  **(c) Decision**  **(i) Proof of solvency**  The presumption of insolvency operates in a defence to a winding up summons. Barrett J stated that Mr Koutsourais thus bears the onus of proof and, referring to Commonwealth Bank of Australia v Begonia (1993) 11 ACLC 477, that the "fullest and best" evidence of the financial position of the company must be lead and, in particular, verification of the assets and liabilities of the company is critical. Citing Expile Pty Ltd v Jabb's Excavations Pty Ltd (2003) 45 ACSR 711, Barrett J noted that "mere assertions by a company's controller as to its solvency and the state of its assets and liabilities are of no real value to the court".  There were insufficient books and records of the company to allow the liquidator to estimate either the quantum or number of creditors. Neither the liquidator nor an external accountant lead evidence to verify the solvency of the company. Further, Barrett J found no evidence of the state of financial account between the company and Mr Koutsourais despite Mr Koutsourais' claim that he owed Bambakit up to $105,160. Barrett J found that the Applicant had provided insufficient evidence to discharge the onus of proof regarding the solvency of Bambakit.  **(ii) "Commercial morality" and "public interest"**  In finding that it would be unacceptable to restore management of Bambakit to Mr Koutsourais, Barrett J highlighted the following:   * Mr Koutsourais failed to see the difference between the company and himself; * Bambakit did not keep adequate books and records; * the likelihood of Mr Koutsourais creating and maintaining appropriate records upon termination of the winding-up is remote; and * Mr. Koutsourais did not deal conscientiously with the responsibilities accruing to him following the making of the winding up order (evidenced in part by the successful prosecution under section 530A of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default)).   Referring to Re Sky Fashions Pty Ltd (1986) 10 ACLR 743 at 746, Barrett J also noted that the possibility of the affairs of the company being conducted "in the same sloppy fashion" as previously was a consideration. Evidence adduced by Ms Metledge, that Mr Koutsourais was conducting his smash repairs business under a business name the registration of which had expired in 1998, demonstrated continuing "sloppy" commercial behaviour.  **(iii) Possible conditions on section 482 order**  Whilst section 482 does not contemplate conditional orders, in obiter, Barrett J acknowledged that section 482(3) empowers the court to give directions for "the resumption of the management and control of the company by its officers" and that this may effectively allow conditional orders.  Barrett J found that it would be inappropriate to grant an application under section 482 subject to Mr Koutsourais' wife and/or children being appointed directors of Bambakit given:   * the lack of reliable means of ensuring compliance because of the close family relationships involved; and * the concept of de facto directors.   **5.9 Construction of costs enforcement clause in mining royalty agreement**  (By Brett Cohen, Solicitor, Clayton Utz)  Precious Metals Australia Limited v Xstrata (Schweiz) AG [2005] NSWSC 147, New South Wales Supreme Court, Einstein J, 9 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc147.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc147.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  Pursuant to a mining royalty agreement, the plaintiff was entitled to a royalty for production carried out at a vanadium mine. The plaintiff instituted proceedings for breach of contract, alleging that the mine's owner purported to permanently close the mine, thereby ceasing royalty payments.  The mining royalty agreement contained a guarantee and indemnity given by the mine owner's holding company for the benefit of the plaintiff in relation to the mine owner's obligations under the mining royalty agreement.  In this case the New South Wales Supreme Court considered the extent to which a costs enforcement clause contained in the mining royalty agreement entitled the plaintiff to an indemnity from the holding company in respect of all costs incurred on the plaintiff's proceedings concerning the alleged breach of the mining royalty agreement by the mine owner.  It was held that the costs enforcement clause in the mining royalty agreement would not permit the plaintiff to hold the guarantor holding company liable for costs incurred in relation to the enforcement or making of invalid claims. The Court stated that if parties intend the terms of an agreement to operate unreasonably, that intention must be made abundantly clear.  **(b) Facts**  On 16 October 2000 Precious Metals Australia Ltd ("PMA"), Xstrata Windimurra Pty Ltd ("Xwin") and Xwin's holding company Xstrata AG ("Xstrata AG") agreed to PMA selling interest in a mining joint venture known as the Windimurra Vanadium Project. By agreement on 16 October 2000, Xwin also agreed to pay PMA a production royalty ("Royalty Agreement").  By clauses 7.1 and 7.2 of the Royalty Agreement Xstrata AG agreed to provide a Guarantee and Indemnity for the benefit of PMA for the performance of Xwin's obligations under the Royalty Agreement.  Clause 7.7(a) of the Royalty Agreement provided that:  "Xstrata AG agrees to pay or reimburse PMA on demand for all costs, charges and expenses in making, enforcing and doing anything in connection with the Guarantee and Indemnity including, but not limited to, legal costs and expenses on a full indemnity basis."  By a Deed of Assignment, Xstrata (Schweiz) AG ("Xstrata") took an assignment of Xstrata AG's rights and obligations under the Royalty Agreement.  PMA commenced proceedings in the New South Wales Supreme Court alleging that, by purporting to permanently close the Windimurra Vanadium Project in early May 2004, Xwin had breached the Royalty Agreement ("Contract Proceedings"). Xstrata was also named as a defendant in the Contract Proceedings. PMA further claimed that it had affirmed the Royalty Agreement which PMA asserted had the effect that the parties to the Royalty Agreement continued to be bound.  PMA also brought these separate proceedings against Xstrata regarding clause 7 of the Royalty Agreement, which PMA said obliged Xstrata to pay or reimburse PMA for all costs and expenses it incurred in connection with the Contract Proceedings including, but not limited to, legal costs and expenses on a full indemnity basis ("Guarantee Proceedings").  The Guarantee Proceedings were commenced by PMA when Xstrata made an application seeking security for costs in the Contract Proceedings. If PMA was successful in the Guarantee Proceedings, the security for costs application would be untenable. The Court converted PMA's motion into a final hearing of the Guarantee Proceedings consensually, with the security for costs decision to be delivered in the Contract Proceedings if required.  In this case the Court separated the following question for determination prior to all other questions in the application: "Whether on the proper construction of clause 7.7(a) of the Royalty Agreement, such Royalty Agreement being considered as a whole, Xstrata is liable to pay or reimburse the costs, charges and expenses as incurred, and [which] may hereafter be incurred by the plaintiff ("PMA") in prosecuting [the Contract Proceedings] against Xwin: · as and when incurred and on demand (that is, before resolution of [the Contract Proceedings]); · whether or not PMA succeeds or is entitled to succeed in that action; and · on an indemnity basis, except insofar as they are of an unreasonable amount or have been unreasonably incurred, so that, subject to the above exceptions, PMA is completely indemnified in respect of the same."  **(c) Decision**  Justice Einstein in the New South Wales Supreme Court found for Xstrata on the first and second separate questions for determination and held that clause 7.7(a) of the Royalty Agreement did not oblige Xstrata to pay PMA's costs incurred in the Contract Proceedings before resolution of that action, nor to pay such costs whether or not PMA succeeds or is entitled to succeed. His Honour stated that submissions would be taken on the need, if any, to answer the question of PMA's entitlement to costs on an indemnity basis in the Contract Proceedings.  His Honour identified the following principles of construction of a written document:   * primacy should be given to unambiguous words used in a written contract; * one should seek to ascertain the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract; and * commercial contracts should be construed so as to be given a sensible commercial operation.   His Honour found that clauses 7.1 and 7.2 of the Royalty Agreement imposed separate promises of guarantee and indemnity on Xstrata and that:   * clause 7.1 imposed an obligation on Xstrata by way of a guarantee to see to it that Xwin performs its obligations under the Royalty Agreement; and * clause 7.2 was a broad indemnity that imposed upon Xstrata liabilities separate from and additional to the liability provided for in the guarantee in clause 7.1.   Justice Einstein observed that if PMA's construction of clause 7.7 was upheld, Xstrata would be liable to indemnify PMA for its costs and expenses incurred in pursuing any actions against Xwin in respect of any of its conduct under the Royalty Agreement, irrespective of whether those actions are good, bad or hopeless.  Justice Einstein considered the meaning of "making, enforcing and doing anything in connection with the Guarantee and Indemnity" contained in clause 7.7(a). His Honour held that this was a composite expression, rather than a disjunctive one, that pertained to making or enforcing a valid claim under the Royalty Agreement. An unsuccessful attempt to enforce or making an invalid claim would not be covered by this expression.  His Honour held that:   * the parties had deliberately chosen the subject matter of clause 7.7(a) to be the specific obligations contained under clauses 7.1 and 7.2; * the parties had refrained from defining the subject matter of clause 7.7(a) more broadly by reference to the obligations of Xwin or Xstrata under the Royalty Agreement; and * the purpose of clause 7.7(a) was to give PMA a costs indemnity where Xstrata does have a liability under clause 7.1 or 7.2.   His Honour noted certain cases concerning attempts by the creditor to hold the guarantor liable for costs incurred in pursuing the principal debtor. His Honour considered that those cases held no support for the proposition that a costs enforcement clause in a guarantee permits the creditor to hold the guarantor liable for failed actions against either the principal debtor or the guarantor.  Justice Einstein observed that in construing written contracts it should be presumed that the parties did not intend the terms of their agreement to operate unreasonably, and that if an unreasonable outcome was intended, that intention should be made "abundantly clear." His Honour stated that "had the parties to the agreement intended that clause 7.7 would require an invalid demand to be honoured, and for the defendant to pay the costs of a wrongful claim to be made against it by the plaintiff, those matters would have been expressly stated."  His Honour held that in the event of any doubt, the Guarantee and the Indemnity should be construed in favour of Xstrata as the guarantor or indemnifier. Finally, his Honour stated that, if the outcome of the Contract Proceedings was such that PMA had sought to enforce what are shown to be its actual legal rights under the Guarantee and/or the Indemnity, then Xstrata would be liable to pay all costs including legal costs incurred in connection with that enforcement.  **5.10 Provisions in Corporations Act dealing with independence of auditors can affect claim for legal professional privilege**  (By James Ogilvy, Blake Dawson Waldron)  789TEN Pty Ltd v Westpac Banking Corporation Ltd [2005] NSWSC 123, New South Wales Supreme Court, Bergin J, 8 March 2005  The full text of this judgement is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc123.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc123.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/index.html](http://cclsr.law.unimelb.edu.au/judgments/index.html" \t "_new)  **(a) Summary**  A Notice of Motion application was brought by Westpac Banking Corporation Limited (Westpac) to prevent 789TEN Pty Ltd (the plaintiff) gaining access to two sets of documents (the KPMG Report and the HDY Letters) produced on subpoena by KPMG Australia Pty Ltd (KPMG). Westpac claimed legal professional privilege over certain documents, and claimed at various stages "litigation privilege" (section 119 of the [Evidence Act 1995 (NSW)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=4459" \t "default) (the Evidence Act)), "advice privilege" (section 118 of the [Evidence Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=4459" \t "default)), and "settlement privilege" (section 131(1)(b) of the [Evidence Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=4459" \t "default)).  The Report was found to be confidential and privileged because its dominant purpose was to assist Westpac's solicitors in providing relevant professional legal services. There was no express or implied consent to disclose the contents of the documents.  The plaintiff gained access to the HDY letters because they did not meet the "dominant purpose" test. Also, Part 2M.4 of the [Corporation Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default), which requires auditor independence, made it very difficult for Westpac to argue that its auditor (PricewaterhouseCoopers (PWC)) was acting as its implied agent when attempting to claim the "advice privilege". Although each case must be decided on its own individual circumstance, Part 2M.4 militates against the concept of an auditor acting as agent for an audited company.  **(b) Facts**  The main proceedings related to the embezzlement of the plaintiff's funds by Colin Alexander (the second defendant) from the plaintiff's account with Westpac. On 30 December 2002, under the threat of legal proceedings, Westpac's solicitors (Allens Arthur Robinson (Allens), retained by Westpac between November 2002 and June 2003) sent a letter to the Company's solicitors agreeing to take steps toward a resolution financial losses, and recovery processes, in a "spirit of full and frank cooperation". Another letter sent by Allens on 24 March 2003 sought agreement by the plaintiff for Westpac to engage KPMG's accounting division to review the plaintiff's files and accounts, under broadly the same terms as applied to the original letter. This Report was to provide Westpac with an idea of the net amount lost by the Company, whether further recoveries were possible, and whether Westpac would be prepared to make a settlement offer. Westpac was to provide its views to the plaintiff on these issues. The plaintiff agreed to the KPMG review.  **(i) The KPMG documents**  The primary focus of this application was the KPMG report (the Report) that formed part of the documents and communications that were produced on subpoena by KPMG. One draft Report was provided to Allens, and the other to Henry Davis York (HDY, retained by Westpac from late June 2003). The plaintiff submitted that it was not privileged because it:   * was not intended to be confidential; and * even it if it was confidential, privilege was denied due to either express or implied consent to disclose it gleaned from the content of the letters and the surrounding circumstances.   Westpac claimed the Report was confidential, that "litigation privilege" and "settlement privilege" applied, and that there was no consent to disclose the Report to the plaintiff.  **(ii) The HDY Letters**  The second focus of this case was certain parts of two letters:   * a letter dated 24 September 2004 from Westpac to HDY requesting HDY to communicate directly with PWC solely in relation to the audit of Westpac (Westpac's letter); and * a letter dated 8 October 2004 from HDY to PWC in response to Westpac's letter, which included an updated directors' description of the matter and billing discussion (HDY's letter).   Westpac relied on the "litigation privilege" and the "advice privilege".  **(c) Decision**  **(i) The KPMG documents - litigation privilege found to exist**  Bergin J denied the plaintiff access to the Report on the basis of litigation privilege, but settlement privilege was not made out. She determined that all the relevant KPMG documents and communications were confidential for the purpose of section 117 of the [Evidence Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=4459" \t "default). This was contrary to the plaintiff's argument that the two letters, and in particular the reference to "spirit of full and frank cooperation", indicated that the Report was to be provided, at least in summary, to it. Bergin J interpreted Westpac's intentions as merely to provide the plaintiff with views and conclusions from the Report, and never to disclose the content of the Report itself.  **(ii) Litigation privilege found with no consent to disclose**  Bergin J analysed the litigation privilege which, if found, would deny the plaintiff access to the contents of any confidential documents that were prepared for the "dominant purpose" of the client being provided with professional legal services relating to the anticipated legal proceeding. Despite the plaintiff's argument that the dominant purpose of the Report was merely for Westpac to receive accounting services, Bergin J found in favour of Westpac. Such a report was crucial to the legal advice the lawyers would give to Westpac, particularly regarding the possibility of settlement. Bergin J affirmed the rule that the dominant purpose need not be the sole purpose.  Bergin J dismissed the Company's submission that there were many factual parallels between this case and Singapore Airlines v Sydney Airports Corporation [2004] NSWSC 380 (Singapore Airlines), by finding that the Report was not to be provided to the plaintiff nor was it to be disclosed to a third party, as was the case in Singapore Airlines. [A recent appeal in the Singapore Airlines case was dismissed: Sydney Airports Corporation Ltd v Singapore Airlines Ltd & Qantas Airways Ltd [2005] NSWCA 47.]  **(iii) Settlement privilege not found**  Although clearly finding that the KPMG documents included communications "between one…of the persons in dispute and a third-party"', Bergin J rejected the idea that the communications or documents occurred or were prepared "in connection with an attempt to negotiate a settlement of the dispute". Such a finding requires evidence of an attempt to resolve the "whole dispute" and not just "some of the issues in the dispute".  **(iv) The HDY Letters: privilege denied**  Bergin J denied that either litigation privilege or advice privilege were made out, and thus access to the HDY letters was granted to the plaintiff.  **(v) Ligation privilege not found**  Bergin J failed to find that the HDY letters were made for the "dominant purpose" of Westpac being provided professional legal services relating to the proceedings. The issue of "dominant purpose" was seen as the "real question" and Bergin J highlighted the importance of looking at the whole of the correspondence to ascertain it. She found that HDY provided a professional legal service when it provided an opinion as to the reasonableness of the directors' estimate of a possible settlement. However, she determined that the provision of HDY's opinion was not the dominant purpose of the letter, rather it was to assist PWC, Westpac and its controlled entities with the audit process.  **(vi) Advice privilege, agency and the independent auditor**  Section 118 could only be applied in this case if it were found that PWC was the agent of Westpac for the purpose of receipt of the HDY letter (Mitsubishi Electric Australia Pty Ltd v Victorian Workcover Authority (2002) 4 VR 33, Batt JA at [8]). Westpac submitted that such agency should be implied from the letters' contents and the surrounding circumstances. Bergin J distinguished a number of cases on the premise that, rather than third parties who are agents of a client providing information to solicitors for advice, this case involved the solicitors (HDY) providing information to a third party (PWC) for an audit.  A crucial factor in the decision was the impact of the "Auditor Independence" requirement of Division 3 of Part 2M.4 of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default). Bergin J stated that, "the fact that the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) requires an auditor to be independent of the audited company weighs against the implication that an auditor stands in the shoes of the audited company as its agent in receiving information from third parties about the company." The statutory impact is fundamental (cf McGregor Clothing Ltd's Trade Mark [1978] FSR 353), and there is nothing in the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) that would have authorised PWC to act as Westpac's agent. Bergin J suggested that for such an agency relationship to exist, there would have to be evidence of some special contract, which was not found here. Moreover, Bergin J highlighted the "perception of independence" provision of section 324CD(1)(b) of the [Corporations Act](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) to suggest that if privileged material were given to an auditor in an agency role for the audit process, "the reasonable person would conclude that the auditor is not capable of exercising objective and impartial judgment in relation to the conduct of the audit of the company."  Bergin J confirmed that a company is at risk if it allows its lawyers to deal directly with the auditors when a letter is sought for the purpose, inter alia, of assessing contingent liabilities in financial accounts. She suggested that greater protection of privileged communications could be attained if the lawyers advised the client, and if the client prepared the letter "excluding privileged material".  **5.11 Voting by a secured creditor who has failed to estimate the value of their security may lead to surrender of the entire security**  (By Arvind Dixit, Corrs Chambers Westgarth)  Young v ACN 081 162 512 [2005] NSWSC 139, New South Wales Supreme Court, Gzell J, 4 March 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc139.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/march/2005nswsc139.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  A secured creditor voted to adjourn a creditors meeting without having included an estimate of the value of her security in her statement of particulars of debt. It was held that where a security holder fails to provide an estimate of the value of their security before voting, it should be inferred that the security holder is voting in respect of the whole of their secured debt. As a result, in this case, the secured creditor was deemed to have surrendered her entire security in accordance with the [Corporations Regulations 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default). The court adopted a strict interpretation of the [Corporations Regulations](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default), in concluding that the entire security had been surrendered, notwithstanding the relatively insignificant nature of the resolution on which the creditor voted.  **(b) Facts**  Mr Young was the liquidator of ACN 081 162 512 Pty Ltd (the company). Mrs Cockerill, who held a fixed and floating charge over the assets of the company, submitted a statement of particulars of debt indicating the value of her security as "not known".  Mrs Cockerill later attended a meeting of creditors of the company in liquidation where a poll was demanded on a motion to adjourn the meeting. Mrs Cockerill voted in favour of the motion. It was concluded by Mr Young that by voting at the meeting, Mrs Cockerill surrendered her entire security under the [Corporations Regulations 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default) reg 5.6.24(3). Mrs Cockerill sought an order reversing Mr Young's decision.  **(c) Decision**  Gzell J found that in the above circumstances, Mrs Cockerill had surrendered her entire security.  The [Corporations Regulations](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default), reg 5.6.24(2), provide that a secured creditor is not entitled to vote at a creditors meeting except to the extent of any balance due to the secured creditor after deducting the value of his or her security, as estimated by the secured creditor. Regulation 5.6.24 provides that for the purposes of voting, a secured creditor must state in the proof of debt, particulars of (among other things) the creditor's estimate of the value of their security.  The statement of particulars of debt submitted by Mrs Cockerill noted her debt as $146,009 but indicated that the value of her security was "not known". Gzell J concluded that in the absence of any estimate provided by the secured creditor as to the value of her security, it should be inferred that the creditor was voting in respect of the whole of her debt.  Under reg 5.6.24(3), if a secured creditor chooses to vote in respect of the whole of their debt, then their security is taken to be surrendered, unless the court is satisfied that the omission to value the security has arisen from inadvertence.  It was submitted by Mrs Cockerill that the failure to value her security arose from inadvertence, hence not falling within the scope reg 5.6.24(3). Gzell J did not accept this submission, and stated that valuing the security as "not known", indicated an inability to determine the value of that security, rather than a failure to value through inadvertence. Therefore Gzell J deemed Mrs Cockerill to have surrendered her security under reg 5.6.24(3).  Gzell J acknowledged that it is unfortunate that a secured creditor may lose their security by voting on a poll which has nothing to do with their security and relates to a "mundane matter" like adjourning a meeting. Gzell J adopted a strict interpretation of the [Corporations Regulations](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56758" \t "default) however, noting that the provisions are mandatory and make no distinction between substantive and non-substantive matters.  **5.12 Liquidators' unsuccessful attempt to disclaim contracts**  (By Mia Livingstone, Articled Clerk, Clayton Utz)  Sims and Singleton as Liquidators of Enron Australia Pty Limited v TXU Electricity Limited [2005] NSWCA 12, New South Wales Court of Appeal, Spigelman CJ, Sheller JA and Brownie AJA, 11 February 2005  The full text of this judgment is available at: [http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/february/2005nswca12.htm](http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2005/february/2005nswca12.htm" \t "_new) or [http://cclsr.law.unimelb.edu.au/judgments/](http://cclsr.law.unimelb.edu.au/judgments/" \t "_new)  **(a) Summary**  The appeal was brought by the liquidators of Enron Australia Finance Pty Ltd (Enron) (Appellants) who sought leave to disclaim contracts with contracting parties TXU Electricity Ltd (TXU) and Yallourn Energy Pty Ltd (Yallourn) (Respondents) worth a total of $3.1 million to the Appellants but only on the basis of the Court making certain orders pursuant to section 568(1B)(b) of the [Corporations Act 2001 (Cth)](http://research.lawlex.com.au/index.asp?pact=coredoc&nav=col&cid=56482" \t "default) (Act). The Appellants were refused leave to disclaim at first instance and appealed the decision on the ground that the Court was empowered under section 568(1B)(b) of the Act to make the orders of the nature sought.  The Appellants argued that section 568(1B) encompassed the making of an order which would alter the contractual rights of the other contracting party. In support of this argument, the Appellants relied upon the general legislative intent of Division 7A of the Act (in which section 568(1B) appears), the breadth of language found in section 568(1B), the structure of section 568(1B), the history of disclaimer provisions in the United Kingdom and Australia and relevant case law. Conversely, the Respondents placed particular reliance on the express terms of section 568D of the Act, which invoked a test of necessity, to argue that the orders sought by the Appellants were not orders "necessary" to release Enron or its property from liability.  The Court held that although the legislative intent of Division 7A is to facilitate the prompt and efficient liquidation of a company and the release of a company from its obligations, the means chosen to achieve that objective are not at large. The Court found that the broad language of section 568(1B)(b) should be read down in light of section 568D so that the effect of a disclaimer on another contracting party's rights or liabilities does not go further than what is "necessary" to release the company or its property from liability. Further, the Court held that neither the legislative history nor case law authorised the Court to make the orders sought by the Appellants. The appeal was dismissed with costs.  **(b) Facts**  Prior to Enron's liquidation, Enron traded in the Australian electricity derivatives market by entering into electricity swap contracts with various counterparties, including the Respondents. At the commencement of Enron's voluntary administration (which later became its liquidation), 78 contracts between Enron and the Respondents remained "open" in the sense that the time for performing the contracts by ascertaining and paying amounts due had not then arrived. The contracts with Yallourn had expired since the judgment at first instance. However, the contracts with TXU remained on foot.  The obligation of TXU to make payments under the contracts was subject to two conditions precedent: that (1) no event of default had occurred and (2) no early termination date had occurred or had been effectively designated. The appointment of voluntary administrators to Enron and the subsequent appointment of liquidators was an event of default which meant that TXU had no obligation to make the payments under the contracts.  The Appellants' case was that Enron had a substantial asset in the contracts but was unable to realise that asset in the absence of a contractual right to designate, or to force TXU to designate, an early termination date. In that event, the Appellants sought leave to disclaim but only on the basis that the Court would make an order under section 568(1B)(b) which had the effect that TXU was taken to have designated an early termination date and, accordingly, would be obliged to pay Enron the value of the contracts.  **(c) Decision**  The appeal was dismissed with costs.  **(i) Relevant law**  Section 568D(1) of the Act states the effect of a liquidator's disclaiming property, in this case the contracts in question. It explains that a disclaimer is taken to have terminated the company's rights, interests, liabilities and property in or in respect of the disclaimer property, but does not affect any other person's rights or liabilities except so far as necessary in order to release the company and its property from liability.  Section 568(1A) provides that a liquidator cannot disclaim a contract (other than an unprofitable contract or a lease of land) without leave of the Court. Section 568(1B)(b) of the Act goes on to provide that, on an application for leave under subsection (1A), the Court may make such orders in connection with matters arising under, or relating to, the contract as the Court considers just and equitable.  **(ii) Reasoning**  In dismissing the appeal, Spigelman CA (with whom Sheller JA and Brownie AJA concurred) rejected the Appellants' contention that section 568(1B) confers on the Court the broad power to make an order that alters the contractual rights of the other contracting party where it is not "necessary" to affect that right in order to release the company or its property from liability.  Although the Court accepted the Appellants' submission that the general legislative intent of Division 7A of the Act is to facilitate the prompt and efficient liquidation of a company, the Court held that the means chosen to achieve that objective are not at large.  The Appellants further argued that their contention was supported by the breadth of the language used in, and the structure of, section 568(1B). In particular, the Appellants relied on the wording that orders may be made "in connection with matters" which may be as wide as merely "relating to" the relevant contract. However, the Court generally agreed with Austin J's reasoning at first instance and read down the broad language of section 568(1B).  The Court held that section 568D provides a context for section 568(1B) which indicates that the section is not intended to authorise the variation of contractual rights and obligations in the manner contended for by the Appellants. In fact, the orders, if made, would deprive the Respondents of their contractual rights under contracts which expressly deal with the consequences of liquidation, to decline to trigger early termination, and of the benefits they would derive from that course. The Court found that such an outcome was not "necessary" to release Enron and its property from liability within the wording of section 568D.  The Appellants also relied on the history of disclaimer provisions in insolvency legislation both in the United Kingdom and in Australia and relevant case law. The Court discussed the case of Re Moser (1884) 13 QBD 738 where Wills J had considered the analogous legislative scheme in bankruptcy law. The Court agreed with Austin J's analysis of Re Moser at first instance to reject the Appellants' appeal, finding that nothing in the judgment of Wills J suggested that his Lordship exercised the power under an equivalent section to 568(1B) in a way which altered the contractual rights of the parties. |
| **6. Contributions** |
| If you would like to contribute an article or news item to the Bulletin, please email it to: "[cclsr@law.unimelb.edu.au](mailto:cclsr@law.unimelb.edu.au)". |
| **7. Subscription** |
| To subscribe to the Corporate Law Bulletin or unsubscribe, please send an email to "[cclsr@lawlex.com.au](mailto:cclsr@lawlex.com.au)". |
| **8. Change of Email Address** |
| [Click here](http://research.lawlex.com.au/" \t "default) to change your profile  LAWLEX welcomes users' suggestions for improving this service. Please contact [Customer Service](mailto:alert@lawlex.com.au). |
| **9. Website Version** |
| As a subscriber, you may view and print the latest Bulletin on the [LAWLEX website](http://research.lawlex.com.au/cclsr/archive" \t "default), from where you can also access previous editions of this bulletin. |
| **10. Copyright** . |
| Centre for Corporate Law and Securities Regulation 2005  You may use this material for your own personal reference only. The material may not otherwise be used, copied or redistributed in any form or by any means without a multiple user licence with LAWLEX. |
| **11. Disclaimer** |
| No person should rely on the contents of this publication without first obtaining advice from a qualified professional person. This publication is provided on the terms and understanding that (1) the authors, editors and endorsers are not responsible for the results of any actions taken on the basis of information in this publication, nor for any error in or omission from this publication; and (2) the publisher is not engaged in rendering legal, accounting, professional or other advice or services. The publisher, authors, editors and endorsers expressly disclaim all and any liability and responsibility to any person in respect of anything done by any such person in reliance, whether wholly or partially, upon the whole or any part of the contents of this publication. |

[Click here](http://research.lawlex.com.au/) to modify your Alert profile.  
To modify your Newsfeed subscription, or for general assistance, please contact [Customer Service](mailto:alert@lawlex.com.au).  
LAWLEX also welcomes users' suggestions for improving this service.

**Disclaimer:** This email alert is not intended to be and is not a complete or definitive statement of the law on the relevant subject matter. No person should take any action or refrain from taking any action in reliance upon the contents of this alert without first obtaining advice from a qualified practitioner. LAWLEX expressly disclaims liability for any loss or damage suffered howsoever caused whether due to negligence or otherwise arising from the use of this information. A complete copy of the disclaimer terms of use and licence agreement is available through the links above this summary. For further information or if you have received this notice in error or believe that the email has been forwarded to you in breach of our licence terms, please notify LAWLEX immediately by telephone on 03 9278 1555 or email alert@lawlex.com.au.

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