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**CONTENTS**

1. [RECENT CORPORATE LAW DEVELOPMENTS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#1.recent)  
(A) [The unravelling of Australia’s Federal corporate law](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28A%29theunravelling)  
(B) [CLERP Act commences](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28B%29clerp)  
(C) [Takeover panellists appointed](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28C%29takeover)  
(D) [Takeovers Panel advice on aspects of new regime](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28D%29takeoverspanel)  
(E) [UK Department of Trade and Industry consultation document on modern company law](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28E%29ukdepartment)

2. [RECENT ASIC DEVELOPMENTS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#2.recentasic)  
(A) [Investors benefit from free "OFFERlist"](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28A%29investors)  
(B) [ASIC’s Interim Policy Statement No 159 on discretionary powers in relation to takeovers](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28B%29asic%27sinterim)

3. [RECENT ASX DEVELOPMENTS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#3.recentasx)  
(A) [Listing rule amendments](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28A%29listingrule)

4. [RECENT CORPORATE LAW DECISIONS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#4.recentcorporatelaw)  
(A)[Commonwealth DPP does not have power to bring appeal against sentence for breach of State law](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28A%29commonwealthdpp)  
(B) [Right to full and absolute ownership is not necessarily a charge](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28B%29righttofull)  
(C) [ASIC powers do not impinge upon the court’s powers to control inspection of documents during proceedings](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28C%29asicpowers)  
(D) [Disclosure requirements for Explanatory Memorandum in members’ scheme of arrangements](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28D%29disclosure)  
(E) [The NRMA judgment – demutualisation under section 411](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#%28E%29thenrma)

5. [RECENT CORPORATE LAW JOURNAL ARTICLES](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#5.recentjournalarticles)

6. [NEW CLERP BOOKS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#6.newclerpbooks)

7. [MELBOURNE UNIVERSITY CORPORATE AND COMMERCIAL LAW SUBJECTS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#7.melbourneuniversity)

8. [ARCHIVES](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#8.archives)

9. [CONTRIBUTIONS](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#9.contributions)

10. [MEMBERSHIP AND SIGN-OFF](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#10.membership)

11. [DISCLAIMER](http://www.law.unimelb.edu.au/bulletins/archive/Bulletin0031.htm#11.disclaimer)

1. RECENT CORPORATE LAW DEVELOPMENTS

(A) THE UNRAVELLING OF AUSTRALIA’S FEDERAL CORPORATE LAW

(By Professor Ian Ramsay, Director, Centre for Corporate Law and Securities Regulation)

As a result of recent judgments, Australia’s Federal structure of corporate law is under substantial challenge. The seriousness of the situation is demonstrated in an Australian Securities and Investments Commission media release of 23 March 2000 in which ASIC Chairman Alan Cameron said that recent judgments "reflect the High Court’s view that the complex, highly technical scheme to create, by agreement, a regime of national regulation by the Commonwealth administering State laws is indeed so complex, that it falls under its own weight". Mr Cameron is quoted as saying that the recent cases demonstrate the need to fix the basic question of company law in Australia once and for all.

This brief Note commences with an overview of the Federal structure of Australia’s corporate law. It then refers to the judgments which challenge this Federal structure and concludes with an examination of possibilities for reform.

(1) Australia’s Federal structure of corporate law

Although many people typically think of Australia’s corporate law as being a national law, the reality is very different. Corporate law is State law but with a number of federalising features. In other words, the Corporations Law is an Act of each of the States. The reason for this lies in the High Court judgment in New South Wales v Commonwealth (1990) 169 CLR 482 where the High Court considered section 51(xx) of the constitution in the context of an attempt by the Commonwealth Government to enact a national Corporations Act. Section 51(xx) gives the Commonwealth Government power to legislate with respect to "foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth". In this 1990 judgment, the High Court (by a majority of 6 to 1) held that section 51(xx) did not confer on the Commonwealth Government power to deal with the incorporation of companies. Only the State governments have this power.

It must be recalled that the Commonwealth Government’s attempt to legislate nationally for the regulation of companies (including the incorporation of companies) followed persistent problems with the previous so-called cooperative scheme which existed from 1982 through to the end of 1990. In 1987 the Senate Standing Committee on Constitutional and Legal Affairs published a Report titled "The Role of Parliament in Relation to the National Companies Scheme" in which the Committee identified a number of substantial problems with the cooperative scheme including lack of uniform administration by the State Corporate Affairs Commissions; lack of accountability; and duplication of functions between the State Corporate Affairs Commissions and the National Companies and Securities Commission. In addition, there were general concerns about the need for more effective national enforcement. The Committee recommended that the Commonwealth Government should assume full responsibility for corporate regulation and this resulted in the enactment of the Corporations Act 1989 (Cth) and the Australian Securities Commission Act 1989 (Cth). However, the High Court judgment in New South Wales v Commonwealth meant that significant parts of the Corporations Act were unconstitutional.

Negotiations between the various State governments and the Commonwealth Government led to an agreement which was signed in June 1990. Each State would enact its own Corporations Act and the Commonwealth Corporations Act would apply only to the Australian Capital Territory and not to the States. However, in order to have a national structure for the regulation of companies, a number of key federalising features were added. Some of the more important are as follows:

(i) the Australian Securities Commission (now the Australian Securities and Investments Commission) was established as the national regulator to assume full responsibility for the regulation of companies. It replaced the State Corporate Affairs Commissions and the National Companies and Securities Commission.

(ii) Federal administrative bodies such as the Administrative Appeals Tribunal and the Commonwealth Ombudsman would have a role to play in corporate regulation.

(iii) The investigation and prosecution of offences under the various State Corporations Acts would be undertaken by ASIC, the Federal police and the Commonwealth Director of Public Prosecutions.

(iv) The Federal Court was given the power to hear matters arising under the State Corporations Acts. This was done by means of cross-vesting legislation.

(v) Any amendments that the Commonwealth Government made to its Corporations Act would automatically apply in each of the States without the need for the State Parliaments to pass further amendments.

(vi) The Commonwealth Government was given enhanced voting on the Ministerial Council (which is constituted by the relevant Commonwealth Government and State Government Ministers) in order to strengthen its role.

In summary, despite the fact that the High Court judgment in New South Wales v Commonwealth meant that the Commonwealth Government did not have the power to deal with the incorporation of companies and therefore there would need to be some form of State companies legislation, a strong effort was made to have national regulation of companies. This structure is now under substantial challenge as a result of several recent judgments.

(2) The recent challenges

(i) Re Wakim

In Re Wakim (1999) 31 ACSR 99; 17 ACLC 1,055, the High Court struck down the cross-vesting legislation referred to above. This judgment is discussed in detail in Bulletin No 22 (<http://cclsr.law.unimelb.edu.au/Bulletins/Bulletin0022.htm>). Although all the State governments and the Commonwealth Government had agreed that it was appropriate for the Federal Court to play a role in disputes arising under the State Corporations Acts, the High Court held that this was unconstitutional on the basis that Chapter III of the Constitution did not allow the State governments, even with the agreement of the Commonwealth Government, to invest Federal courts with State jurisdiction.

The effect of this judgment has been to eliminate virtually all of the Federal Court’s jurisdiction to hear matters arising under the State Corporations Acts. The implications of the decision have been profound. First, in order to overcome the threat that all previous judgments of the Federal Court dealing with State Corporations Act matters are invalid, the State governments have passed what can be described as emergency legislation to deem these previous Federal Court decisions to be decisions of the various State Supreme Courts and therefore valid. However, there are currently at least two challenges to these validating Acts and these challenges are expected to be heard by the High Court in May.

Secondly, cases commenced in the Federal Court prior to the Re Wakim judgment needed to be recommenced in the relevant State Supreme Court with additional costs imposed upon the parties. Thirdly, we have seen a substantial number of judgments since Re Wakim in which courts have endeavoured to more clearly identify what jurisdiction remains with the Federal Court and there is still uncertainty in relation to this important issue. Fourthly, a number of commentators have found it regrettable that the Federal Court, which had built up over the course of the last ten years considerable expertise in corporate law matters (and often was quicker in terms of being able to hear such matters than a number of the State Supreme Courts), is now effectively precluded from hearing these matters. Finally, some commentators have also found it regrettable that the situation which had successfully worked for the previous ten years of allowing litigants in matters arising under the State Corporations Act to have a choice of courts (the Federal Court or the relevant State Supreme Court) no longer exists.

(ii) Bond v The Queen

A further challenge to the Federal structure of Australia’s corporate law has resulted from the decision of the High Court in Bond v The Queen on 9 March of this year. This judgment is the subject of detailed comment later in this Bulletin (see Item 4(A)). In brief, the High Court held that the Commonwealth Director of Public Prosecutions does not have the power to appeal against a sentence imposed for a breach of a State Corporations Act. The Commonwealth DPP does have the power to initiate and institute prosecutions for such breaches, but it does not have power to appeal against sentences. As a result of this judgment, such appeals will need to be instituted by the relevant State DPP.

(iii) The Queen v Hughes

The most substantial challenges to the Federal structure of Australia’s corporate law was heard by the High Court on the 1st and 2nd of March 2000, with judgment expected later this year. The case is The Queen v Hughes. It has been the subject of considerable media commentary in the last few days and this interest is understandable for reasons explained below.

The case turns on the validity of section 45 of the Corporations (Western Australia) Act 1989. Section 45 states that an offence against the State Act is taken to be an offence against the laws of the Commonwealth. This is an important provision because it is the basis for the Commonwealth Director of Public Prosecutions having the power to prosecute offences arising under the State Corporations Acts. The challenge in the High Court goes to the constitutional validity of section 45. While the judgment of the High Court cannot be predicted, it would be true to say from a reading of the 100 page transcript (which is available on the website of the High Court at (http://www.hcourt.gov.au) that several of the judges expressed significant doubt about the validity of section 45.

Should section 45 be struck down, the implications are profound. Not only will the Commonwealth Director of Public Prosecutions no longer have a role to play in prosecuting breaches of State Corporations Acts under the current regime, but there is a real question as to the role and authority of the Australian Securities and Investments Commission in terms of its powers to investigate breaches of the State Corporations Acts.

Even if section 45 is upheld by the High Court, one can safely predict further challenges to the constitutional validity of our existing corporate structure.

(3) Some possible solutions

What solutions might there be to the unravelling of the Federal structure of corporate regulation? One possibility is a Referendum to amend the Constitution to grant enhanced power to the Commonwealth Government in relation to corporate regulation. The difficulty with this solution is that the majority of proposals to amend the Constitution have failed.

A second possibility is a referral by each of the State governments to the Commonwealth Government of their power to regulate companies. Such a referral is permitted under section 51(xxxvii) of the Constitution. However, in the past week, the Attorneys-General of the States of Western Australia and South Australia have indicated opposition to a referral. However, just because one or two States do not refer their power to the Commonwealth does not stop the other States from referring their power. If a majority of States did this the remaining States might quickly fall into line if they realised that substantial costs would be imposed on companies which are incorporated within their State boundaries if they did not join the national scheme. It may be, for example, that companies incorporated in these States would need to register as foreign corporations in the States which had joined the national scheme in order to conduct business in those States. The concept of companies incorporated in one State being required to register as a foreign company in another State in which the company wanted to do business was required under earlier companies legislation.

A third possibility would be for there to be a split system of regulation between the State governments and the Commonwealth. State governments would regulate the incorporation of companies and possibly some other matters while the Commonwealth Government would regulate matters such as takeovers and fundraising by companies. Australia would not be the first country to have such a system. In the United States, there is a split system of regulation with each of the 50 states regulating the incorporation of companies and other matters while the Securities and Exchange Commission (the Federal Government’s regulatory agency) deals with other matters such as fundraising by companies. Whether such a split system would work in Australia must be subject to some doubt, particularly given the uncertainty as to where the power of the State governments to regulate companies ceases and where the power of the Commonwealth Government to do so commences. A number of the issues associated with State Government versus Commonwealth Government regulation of companies are examined in several articles: M Whincop, ‘The Political Economy of Corporate Law Reform in Australia’ (1999) 27 Federal Law Review 77 and I Ramsay, ‘Company Law and the Economics of Federalism’ (1990) 19 Federal Law Review 169.

(4) Conclusion

Few would doubt that Australia’s Federal system of corporate law has worked successfully for the past decade. Not everyone may be fully satisfied but we no longer hear the substantial complaints that we did in the 1980s about a lack of uniform administration of companies legislation and ineffective enforcement. The judgments referred to in this brief Note together with The Queen v Hughes, currently before the High Court, pose substantial challenges to our existing system of corporate regulation. Inevitably, the solution lies with a negotiated settlement between the State governments and the Commonwealth Government. One hopes that the solution is reached quickly.

(B) CLERP ACT COMMENCES

The major parts of the Corporate Law Economic Reform Program Act 1999 commenced operation on 13 March 2000. The following is a summary of the more significant changes.

(1) Directors’ duties and shareholders’ remedies

(i) Reformulation of the statutory duty of care of directors and officers of a corporation and the introduction of a statutory business judgment rule to apply to the duty of care and diligence.

(ii) Reformulation of the statutory duty of honesty of directors and officers into a duty to act in good faith in the best interests of the corporation and for a proper purpose.

(iii) A new statutory provision permitting delegation by directors and reliance by directors on information provided by others.

(iv) A new statutory provision allowing a director of a wholly-owned subsidiary who acts in the interests of the holding company to be deemed to act in the best interests of the subsidiary if certain requirements are met.

(v) The introduction of a statutory derivative action and abolition of the common law rules relating to Foss v Harbottle.

(2) Fundraising

(i) Expansion of the exemptions from the prospectus requirements to permit small and medium sized enterprises to raise funds more cheaply and to expand the circumstances where "sophisticated" investors are deemed not to require the protection of a prospectus.

(ii) Revision of the prospectus disclosure requirements to permit fundraising up to $5 million by a short Offer Information Statement and also to permit a short Profile Statement to be distributed instead of a prospectus for certain industries which ASIC thinks are appropriate for this type of disclosure.

(iii) Removal of the requirement that a prospectus be registered rather than merely lodged and facilitation of fundraising and disclosure in electronic form.

(iv) Clarification and simplification of the liability provisions in respect of fundraising, particularly in relation to defences.

(3) Takeovers

(i) Expanding the role and responsibilities of the Corporations and Securities Panel (the Takeovers Panel) by removing the jurisdiction of the courts with respect to determinations during the period of a takeover bid, except where an application is made to the court by ASIC.

(ii) Clarification of the scope of the basic prohibition on acquisitions of shares beyond the 20 per cent threshold, and exemptions from the prohibition.

(iii) Replacement of Part A, B, C and D Statements with a Bidder’s Statement and a Target’s Statement.

(iv) Extension of the takeover provisions to listed managed investment schemes.

(v) Simplifying the requirements for compulsory acquisition after a takeover bid and permitting the acquisition of convertible securities.

(vi) Permitting a 90 per cent holder of securities to compulsorily acquire the outstanding securities of that class.

The "mandatory bid rule" was removed from the Bill during the Parliamentary debates. This rule would have permitted a bidder to cross the 20 per cent threshold by a single acquisition provided that a follow-up bid was made to other target shareholders. The Parliamentary Joint Committee on Corporations and Securities has, this month, been holding hearings on the mandatory bid rule.

There are two new books on the CLERP Act. See Item 6 of this Bulletin for details.

(C) TAKEOVER PANELLISTS APPOINTED

On 9 March 2000 the Minister for Financial Services & Regulation, the Hon Joe Hockey announced the appointment of 17 new members of the Corporations and Securities Panel.

The Panel’s new members are Robyn Ahern, Annabelle Bennett SC, Michael Burgess, Peter Cameron, Maria Manning, Louise McBride, Marian Micalizzi, Professor Ian Ramsay, Maxine Rich, Trevor Rowe, Jeremy Schultz, Jennifer Seabrook, Valentine Smith, Leslie Taylor, Michael Tilley, Karen Wood and Peter Young.

The panel is based in Melbourne and is headed by Simon McKeon from Macquarie Bank. The new appointees will work alongside the Panel’s 11 existing members announced last year.

Major changes to the Corporations Law started on 13 March 2000 under the CLERP Act. These changes streamline the resolution of takeover disputes in Australia. The panel has replaced the courts as the principal body dealing with takeover disputes.

A major feature of the new CLERP legislation is that any party to a takeover is now able to ask the Panel to declare that circumstances surrounding a takeover are unacceptable. The Panel is now also the forum for review of Australian Securities and Investment Commission takeover decisions, a function previously performed by the Administrative Appeals Tribunal.

The Corporations and Securities Panel members:

Ms Robyn AHERN,\* Managing Director, Aherns,WA  
Ms Elizabeth ALEXANDER AM, Partner, PricewaterhouseCoopers, VIC  
Ms Annabelle BENNETT SC,\* Barrister, NSW  
Mr Michael BURGESS,\* Senior Partner, KPMG, SA  
Mr Denis BYRNE, Director, Byrne & Associates, QLD  
Mr Peter CAMERON,\* Partner, Allen, Allen & Hemsley, NSW  
Mr Brett HEADING, Partner, McCullough Robertson, QLD  
Ms Meredith HELLICAR, CEO, Corrs Chambers Westgarth, NSW  
Mr Graham KELLY, Independent Director, NSW  
Ms Maria MANNING,\* Company Secretary, Queensland Cotton, QLD  
Ms Louise McBRIDE,\* Partner, Deloitte Touche Tohmatsu, NSW  
Ms Alice McCLEARY, Independent Director, SA  
Mr Simon McKEON, (President) Executive Director, Macquarie Bank, VIC  
Ms Marian MICALIZZI,\* Partner, PricewaterhouseCoopers, QLD  
Mr Simon MORDANT, Managing Director, Caliburn Partnership, NSW  
Mr John O’NEILL, Managing Director & CEO, Australian Rugby Union, NSW  
Professor Ian RAMSAY,\* Professor of Law and Director of the Centre for Corporate Law and Securities Regulation, The University of Melbourne, VIC  
Ms Maxine RICH,\* Company Director, NSW  
Ms Fiona ROCHE, Managing Director, Estates Development Co, WA  
Mr Trevor ROWE,\* Chairman & Managing Director, Salomon Smith Barney, NSW  
Ms Jennifer SEABROOK,\* Director, Gresham Partners, WA  
Mr Jeremy SCHULTZ,\* Managing Partner, Finlaysons, SA  
Mr Valentine SMITH,\* Former Managing Partner, Dobson, Mitchell & Allport, TAS  
Mr Leslie TAYLOR,\* General Counsel, Commonwealth Bank of Australia, NSW  
Mr Michael TILLEY,\* Managing Director, Investment Banking, Merrill Lynch International, VIC  
Ms Nerolie WITHNALL, Partner, Minter Ellison, QLD  
Ms Karen WOOD,\* Company Secretary, Bonlac Limited, VIC  
Mr Peter YOUNG,\* Executive Vice-Chairman, ABN-AMRO, NSW

\* Indicates new appointment.

(D) TAKEOVERS PANEL ADVICE ON ASPECTS OF NEW REGIME

On 9 March 2000 the Corporations and Securities Panel advised that it will generally require a bidder’s statement for a scrip bid under new Chapter 6 of the Corporations Law to contain the type of information that would be required in a prospectus issued by the bidder for the securities offered as consideration. This is both the intention of Parliament and a reasonable requirement for offerees to make of offerors.

In accordance with this policy, it is likely that the Panel will generally declare circumstances unacceptable if a bidder under a scrip bid, in reliance on a reading of section 636 which goes against the policy of the provision, withholds information which it would have to provide in a prospectus. In consequence, the Panel will also likely order the bidder to obtain and provide any such information which is available to it and its related bodies.

The Panel developed this policy after practitioners drew its attention to new section 636(1)(g) of the Corporations Law, which requires a bidder's statement for a scrip bid to contain the type of information specified in sections 710 to 713 (‘prospectus information’) about the securities offered as consideration, if the bidder is, or controls, the issuer of that scrip.

Often, the issuer of the scrip does not make the bid itself, but causes a subsidiary to make the bid. On one view, the words of section 636(1)(g) do not apply to this situation, because the issuer controls the bidder, not the other way about. An alternative view is that the section will often apply, because the issuer will be a bidder because it is a person who causes or authorises the making of the offers under the bid (see sections 9 and 52).

The policy of section 636 can be seen from the note to section 708(18) and from the relevant Explanatory Memorandum, which says that 'a bidder's statement for a bid offering securities as consideration must contain information for a prospectus offering those securities'. That policy is that prospectus information should be provided whenever scrip is offered as consideration for a bid, and the bidder and the issuer of the scrip are under the same ultimate control.

The same result flows from the more general policy of section 602(a), that takeovers should take place in an efficient, informed and competitive market, and (b)(iii), that shareholders should be given enough information to assess the merits of a proposal under which a person would acquire a substantial interest in the company. To make an informed decision whether to accept a scrip offer, offerees need prospectus information about the bidder’s scrip.

The Panel is considering whether to make a rule under section 658C of the Corporations Law in relation to this issue. The rule would supplement section 636 to ensure that the intentions expressed in the Explanatory Memorandum, and the general policy of section 602 are achieved. The rule would require that whenever scrip is offered as consideration for a bid, and the bidder and the issuer of the scrip are under the same ultimate control, the bidder’s statement must contain the type of information specified in sections 710 to 713.

The Panel invites comments as to whether any such rule is now necessary or appropriate. A draft rule would be issued for comment, before any rule was made. The Panel also invites comment as to whether it would be appropriate to deter such inappropriate conduct by a rule or by inclusion in a Panel policy statement on unacceptable circumstances.

The Panel notes the Information Release published by the Australian Securities and Investments Commission on 7 March 2000. The Panel has consulted with ASIC and the Department of Treasury in developing this policy.

Submissions or comments on this matter should be sent to:

The Executive  
Corporations and Securities Panel  
GPO Box 5179AA  
Melbourne,  
VIC, 3001

or emailed to: "takeovers@takeovers.gov.au".

For further information contact:

Nigel Morris  
Corporations and Securities Panel  
Tel: (03) 9280 3299

(E) UK DEPARTMENT OF TRADE AND INDUSTRY CONSULTATION DOCUMENT ON MODERN COMPANY LAW

Earlier this month the UK Department of Trade and Industry released a Consultation Document from its Company Law Review Steering Group titled "Modern Company Law for a Competitive Economy: Developing the Framework".

It is the second Consultation Document issued by the Steering Group. The first, issued in February 1999, titled "Strategic Framework Consultation Document" set out the terms of reference and principles on which the Review was to be based and analysed and made proposals on a number of areas for initial consultation. That was followed by three more documents in October 1999 on company general meetings and shareholder communication; formation and capital maintenance; and overseas companies.

The latest Consultation Document analyses and makes proposals on key areas of corporate governance (that is, the main rules governing the operation and control of companies) and special consideration is given to small and private companies. Responses are sought by 15 June in relation to the proposals on small and private companies and 28 July on the remainder of the proposals.

The document deals with such issues as:

(i) In whose interests should companies be run? The Steering Group argues that the overall objective of wealth generation and competitiveness for the benefit of all is best achieved through wider public accountability (achieved principally through improved company reporting) and an "inclusive" approach to directors’ duties which requires directors to have regard to all the relationships on which the company depends and to the long, as well as the short-term implications of their actions, with a view to achieving company success for the benefit of shareholders as a whole.

(ii) A legislative re-statement of directors’ duties.

(iii) Reform of the remedies available to minority shareholders including derivative actions and improvements in rules on notice, timing, agendas, voting and resolutions for general meetings.

(iv) Enhanced reporting and accounting requirements for listed and other large companies including a proposal that for public and very large private companies, there be a requirement that the full annual report include a new statutory operating and financial review, which would enable the user to assess the performance and prospects of the business, including its wider relationships (eg with employees and suppliers), its reputation and its impact on the community and the environment.

(v) Simplification of the law for private companies and a set of new provisions specifically designed to suit the needs of small companies (such as simplifying the capital maintenance rules and removing the requirement to have a company secretary as well as making provision for arbitration of shareholder disputes and simplifying the model constitution). Also proposed is a simpler form of report and accounts to be satisfied by small companies.

The Consultation Document is available from the Department of Trade and Industry website at:

"<http://www.dti.gov.uk/cld/modcolaw.htm>".

2. RECENT ASIC DEVELOPMENTS

(A) INVESTORS BENEFIT FROM FREE "OFFERLIST"

On 14 March 2000 ASIC Chairman Mr Alan Cameron launched OFFERlist which will give investors access to details of all offer documents lodged with ASIC. OFFERlist is accessible to the public free of charge through ASIC’s website at "<http://www.asic.gov.au>".

ASIC designed this database to help both fundraisers and the market by allowing the distribution of disclosure documents to the market within the exposure period contained in the new requirements of the Corporate Law Economic Reform Program (CLERP) Act which became effective on 13 March 2000.

OFFERlist gives people the opportunity to obtain and assess the disclosure documents during the exposure period, during which securities cannot be issued.

If offerors give details of where the document can be obtained, the exposure period will be seven days. If, however, these details are not provided ASIC may extend the exposure period to 14 days so that the public can access the document through ASIC’s Document Imaging system.

Offerors are encouraged to provide URL links from ASIC’s OFFERlist site to their own internet home page where the document is displayed.

Mr Cameron said OFFERlist gives investors the opportunity to find out how to access all prospectuses, short form prospectuses, offer information statements and profile statements which have been lodged with ASIC. "OFFERlist should enable the public to request or access disclosure documents and examine the documents during the exposure period and if they have any concerns about the information disclosed in them they can contact ASIC to discuss these with us," Mr Cameron said. "ASIC will assess the validity of the complaints and take appropriate action if necessary."

(B) ASIC’S INTERIM POLICY STATEMENT NO 159 ON DISCRETIONARY POWERS IN RELATION TO TAKEOVERS

On 8 March 2000 ASIC released an interim policy statement on the areas which ASIC expects it will commonly be requested to exercise its discretionary powers in relation to takeovers following the commencement of the Corporate Law Economic Reform Program Act 1999 (CLERP Act) on 13 March 2000.

Interim Policy Statement 159 "Takeovers: discretionary powers" has been prepared after public consultation on the "Policy Proposal Paper: Takeovers: Discretionary Powers" released in August last year.

ASIC expects to replace this interim policy statement with a final policy statement after after it has had an opportunity to monitor the operation of the new Law and policy for an extended period (probably of about 12 months).

The interim policy statement indicates which of ASIC’s existing policies on takeovers will continue to apply after 13 March 2000. ASIC’s approach has been to continue to apply existing policy unless changes brought about by the CLERP Act necessitate a different approach.

(1) Approved exchanges

The 8 March release announces that ASIC will consider approving foreign exchanges for the purposes of the downstream acquisition exception (item 14 of s 611) to the takeovers prohibition on a case by case basis.

ASIC proposes to approve those stock exchanges which require bodies on their official list to comply with takeovers rules or regulations which offer a level of investor protection comparable to that offered in Australia.

From time to time ASIC will announce those exchanges which have been approved for the purposes of the downstream acquisition exception.

In applying for the approval of a particular exchange, applicants should provide ASIC with:

- the content of the actual takeovers rules which the upstream acquisition was subject to;

- information about whether the stock exchange on which the upstream company was listed requires companies on its official list to be subject to a particular takeovers regime (as opposed to allowing the takeover of the listed company to be subject to, for example, the laws of the jurisdiction in which the company is incorporated or the constitution of the company).

ASIC’s policy on downstream acquisitions in Policy Statement 71 will continue to apply to the extent that it is not inconsistent with the new takeovers provisions.

(2) Class orders and prescribed forms ASIC will issue:

- three new class orders referred to in the interim policy statement; and

- revised class orders where it currently provides class order relief from the takeovers provisions;

- new and revised prescribed forms as a result of the CLERP Act.

(3) Issues Papers

ASIC also expects to release issues papers later this year on:

- the minimum bid price rule in s 621(3); and

- false and misleading statements made during takeovers.

(4) Set out below is a summary of the main issues raised in the interim policy statement which introduce new policy or a change to existing policies.

(a) Approval of nominees: ASIC may give relief to approve a nominee appointed under s 615 and s 619(3) that is a licensed securities dealer or a subsidiary of a licensed securities dealer.

(b) Classes of securities: For the purposes of the takeover provisions, ASIC will treat securities as being in the same class in circumstances where:

(i) they would also be characterised as being in the same class for the purposes of the scheme of arrangement provisions; and

(ii) an equitable cash adjustment can be made to the price offered for the different securities.

(c) Securities issued during the currency of an off-market bid: ASIC may give relief to allow an off-market bid to extend to securities issued during the bid period under circumstances which are not within s 617(2), provided the bidder discloses that its bid is extended in this way in its bidder’s statement.

(d) Changes to a bidder’s statement between lodgement and dispatch: In circumtances where an initial bidder’s statement has been lodged with ASIC but not sent to security holders, ASIC will give relief by class order to allow a bidder to send a "replacement bidder’s statement" (being a single document incorporating the initial bidder’s statement as supplemented by the supplementary bidder’s statement) to security holders instead of requiring the bidder to send the initial bidder’s statement and the supplementary statement to the security holders. Where the bid is an off-market bid, the replacement bidder’s statement must be sent to security holders no earlier than the minimum 14 days from the day the replacement bidder’s statement is sent to the target, unless the target or ASIC otherwise agree in writing to a shorter period.

(e) Variation to allow a conditional increase in consideration: ASIC may give relief to allow a bidder during the bid period to offer to increase the consideration to be paid to security holders subject to a minimum acceptance condition, provided that the bidder does not pressure the security holders into accepting the bid by requiring that the minimum acceptance condition be met at a point in time prior to the close of the bid and the bidder is required to pay the increased consideration, even if the minimum acceptance condition is waived.

(f) Notice by 85% holder: ASIC has given class order relief such that s 665D(3) and s 665D(4) do not apply to require a person to give a notice to a company which has only one member or which is a wholly owned subsidiary.

Copies of the interim policy statement and the new class orders can be obtained from ASIC Infoline on 1300 300 630 and from the Policy and Practice Page of the ASIC website at "<http://www.asic.gov.au>".

3. RECENT ASX DEVELOPMENTS

(A) LISTING RULE AMENDMENTS

Listing rule amendments for the Corporate Law Economic Reform Program Act 1999 took effect simultaneously with the Act on 13 March 2000, and have been distributed to listing rule subscribers. The amendments are minor amendments to adopt terminology consistent with the Act, and do not involve policy issues. The package of amendments includes updated Guidance notes and a revised form for directors’ disclosure under section 205G (previously section 235).

Listing rule amendments to introduce quarterly cash flow reports for entities admitted under the assets test on the basis of "commitments" will take effect on 31 March 2000. They are substantially in the form of the proposed amendments exposed for public comment in January 2000.

4. RECENT CORPORATE LAW DECISIONS

(A) COMMONWEALTH DPP DOES NOT HAVE POWER TO BRING APPEAL AGAINST SENTENCE FOR BREACH OF STATE LAW

(By Jürgen Kurtz, Centre for Corporate Law and Securities Regulation, The University of Melbourne)

Bond v The Queen [2000] HCA 13, High Court of Australia, 9 March 2000.

The full text of this judgment is available at:

"<http://cclsr.law.unimelb.edu.au/judgments/states/high/2000/march/2000hca13.html>"

or "<http://cclsr.law.unimelb.edu.au/judgments/>".

(1) Introduction

The unanimous decision of the High Court in this case led to the recent release of Mr Alan Bond from Karnet Prison Farm outside of Perth. The case deals with an appeal by Mr Bond against a custodial sentence imposed by the Court of Criminal Appeal of Western Australia for breaches of the Companies (Western Australia) Code (the "WA Code") (the predecessor to the current Corporations (Western Australia) Act 1990 (WA)).

Like the decision of the High Court in Re Wakim (see [Bulletin No 22](http://cclsr.law.unimelb.edu.au/Bulletins/Bulletin0022htm) for discussion of Re Wakim), this case considers the constitutional relationship between Commonwealth and State laws within the current Corporations Law scheme. Beyond the dry and often technical legal questions in this case, the underlying issues are (in the words of the High Court) "of considerable and general public importance, which go beyond the construction of the particular statutory provisions…involved".

Moreover, since Re Wakim and this case, challenges to the constitutional basis for the Corporations Law scheme have continued. The most recent (and potentially important) challenge is currently before the High Court in R v Hughes.

(2) Factual background

In March 1996, Mr Bond was charged with two counts of breaching sections 229(1)(b) and 570 of the WA Code. (Mr Bond was also charged with breaching section 412 of the Criminal Code (WA) but as this charge is not considered in great detail by the High Court, it will not be considered further in this note). The former charges related to the actions of Mr Bond as an officer of Freefold Pty Ltd between 1988 and 1989. They alleged that Mr Bond had failed to act honestly in the exercise of his powers and the discharge of his duties as an officer of that company. The Commonwealth Deputy Director of Public Prosecutions signed the indictment for these charges.

In early 1997, Mr Bond pleaded guilty in the Supreme Court of Western Australia to the charges that he had breached the WA Code. Murray J sentenced Mr Bond to 3 years’ imprisonment on each of the two counts. It was ordered that the sentence be served partly cumulatively. The total effective sentence was 4 years’ imprisonment to be served cumulatively on top of an existing sentence.

On 21 February 1997, the Commonwealth Director of Public Prosecutions ("DPP") served a notice of appeal against the sentences imposed on Mr Bond. On 22 August 1997, the Court of Criminal Appeal of Western Australia allowed the appeal and resentenced Mr Bond to a total of 7 years’ imprisonment to be served cumulatively on top of an existing sentence.

Mr Bond appealed to the High Court in this case against the decision of the WA Court of Criminal Appeal. The basis for the appeal was that the Commonwealth DPP did not have the authority to institute the appeal to the WA Court of Criminal Appeal against the original sentence imposed by Murray J.

(3) Background to the Corporations Law scheme

Before considering the reasoning of the High Court in this case, it is worth briefly revisiting the structure of the Corporations Law scheme. That structure contains both Commonwealth and State and Territory legislation.

The main pieces of Commonwealth legislation within the scheme are the Corporations Act 1989 (Cth) (as amended) and the Australian Securities and Investments Commission Act 1989 (Cth) (as amended). Section 82 of the Corporations Act 1989 (Cth) sets out the text of the Corporations Law. For constitutional reasons, the Corporations Act 1989 (Cth) applies the Corporations Law in the Australian Capital Territory.

In order to create a hybrid national system, there is identical legislation in each of the States and the Northern Territory which provide that section 82 of the Corporations Act 1989 (Cth) applies as a law of the respective States and Territory. In Western Australia, the Corporations (Western Australia) Act 1990 (WA) is that piece of legislation. It is the provisions of that Act which are considered in part by the High Court in this case.

Aside from the substantive provisions of the Corporations Law, these various forms of legislation also set up the administrative framework for the operation of the scheme. For example, section 91(1) of the Corporations (Western Australia) Act 1990 (WA) provides that the Commonwealth DPP has "enforcement powers" in relation to the Corporations Law of Western Australia. Again, this provision is considered by the High Court in this case.

(4) The decision

The starting point in the reasoning of the High Court was its decision in Re Cram; Ex parte NSW Colliery Proprietors’ Association Ltd (1987) 163 CLR 117. That case found that a Commonwealth Act in general will be construed as requiring a Commonwealth officer to exercise only such powers as the Commonwealth Parliament has chosen to vest in them. A State law which purports to grant some wider power to that officer will be inconsistent with the Commonwealth law. By virtue of section 109 of the Commonwealth Constitution, this will mean that the State law (to the extent of the inconsistency) will be invalid.

The High Court then went on to consider the source of any authority for the Commonwealth DPP to institute an appeal against Mr Bond’s original sentence. It considered both Commonwealth and State law.

(i) State law

The High Court dealt firstly with State law in the form of section 91(1) of the Corporations (Western Australia) Act 1990 (WA). That section provides the Commonwealth DPP with "the same enforcement powers in relation to the [WA Code] as has the Crown in right of the State of Western Australia acting by the Attorney General or such other person as may be prescribed by regulations". "Enforcement powers" in turn are defined in section 91(5). The list of powers in that section (such as investigating and prosecuting an offence) do not include instituting an appeal against a sentence. Accordingly, it was found that State law in the form of the Corporations (Western Australia) Act 1990 (WA) did not authorise the Commonwealth DPP to institute an appeal against an existing sentence.

(ii) Commonwealth law

The High Court then went on to consider the position under Commonwealth law. Under section 17 of the Director of Public Prosecutions Act 1983 (Cth) ("DPP Act"), the Commonwealth DPP has the authority to "institute and carry on, in accordance with the terms of the appointment [ie. the appointment to prosecute offences against the laws of a state], prosecutions for such offences".

The High Court noted that ordinarily the next step in an analysis of the ability of the Commonwealth DPP to take a certain course of action would be the exact terms of the State appointment. However, in this case, the High Court held that commencement of prosecutions and commencement of appeals are distinct steps. It held that section 17 did not in any way authorise the Commonwealth DPP to institute appeals (thereby making it irrelevant whether a particular State law conferred such a power on that officer). The Court advanced a number of reasons in support of this conclusion:

- Textual indications: The Court noted that the terms of the Commonwealth DPP Act generally distinguish between the power to institute and carry on (and in some cases, take over) prosecutions and the right (or power) to appeal. This is exhibited in the text of section 17 of that Act as well as other sections (especially section 9(7)).

- The exceptional nature of prosecution appeals: The High Court also based its decision on a broader, jurispudential line of reasoning. In brief, the Court categorised the jurisdiction to appeal against an alleged inadequacy of sentence as an exceptional jurisdiction. This is on the basis that such an appeal places in jeopardy for a second time the freedom of a respondent beyond the sentence imposed. The Court noted that originally this power could only be invoked by the various State Attorneys-General who took political responsibility for their decisions. Given the exceptional nature of such appeals, the Court held that section 17 should not be interpreted as permitting a State to confer on the Commonwealth DPP the power to appeal against a sentence. The States were held to be limited in the power which they may confer on the Commonwealth DPP. That power is the right to institute and carry on prosecutions for offences against a law of a State. In obiter, the Court noted that a State law which confers wider powers (such as the right to appeal a sentence) is inconsistent with Commonwealth law (section 17 of the Commonwealth DPP Act) and will be invalid.

On the basis of this reasoning, the High Court held that the appeal instituted by the Commonwealth DPP against the sentence imposed on Mr Bond by Murray J should be dismissed as incompetent. The High Court went on to set aside the order of the WA Court of Criminal Appeal which was based on that appeal and which led to the increase in Mr Bond’s original sentence.

(5) Implications

The creation of the Corporations Law scheme in 1990 was an attempt to create a uniform set of State and Territory company laws intended to operate largely as national laws. The importance of uniformity in this approach was reinforced by efforts to ensure that those laws would, as far as possible, be administered and enforced on a national basis. National administration and enforcement is the aspect of the Corporations Law scheme which has recently been eroded. The decision of the High Court in Re Wakim has constrained significantly the ability of the Federal Court to determine matters arising under the Corporations Law. This case in turn draws a line in the sand on the enforcement of prosecution for breaches of the Corporations Law. The Commonwealth DPP (together with ASIC) retains the ability to initiate and institute prosecutions for such breaches. However, any decision to appeal against a sentence imposed for such a breach will now be the sole province of the various State and Territory DPPs. It remains to be seen how far this will effect uniformity and consistency of approach to the question of instituting such appeals.

(B) RIGHT TO FULL AND ABSOLUTE OWNERSHIP IS NOT NECESSARILY A CHARGE

(By Adam Brooks, Solicitor, Herbert Geer & Rundle)

D’Aloia & Handberg v Jarvie [2000] VSC 16, Supreme Court of Victoria, Mandie J

2 February 2000.

The full text of this judgment is available at:

"<http://cclsr.law.unimelb.edu.au/judgments/states/vic/2000/february/2000vsc16.html>"

or "<http://cclsr.law.unimelb.edu.au/judgments/>".

Mr D’Aloia and Mr Handberg purported to be the administrators of Smarter Way (Aust) Pty Ltd and were the applicants in this proceeding. The respondent (Mr Jarvie) was the sole director and shareholder of Smarter Way, an internet service provider.

Messrs D’Aloia and Handberg sought an order that Mr Jarvie deliver up the assets and books of Smarter Way. This matter raised a threshold issue; was the administrator validly appointed?

Section 436C(1) of the Corporations Law provides:

"A person who is entitled to enforce a charge on the whole, or substantially the whole, of a company’s property may by writing appoint an administrator of the company if the charge has become, and still is, enforceable".

Mr Jarvie argued that no charge existed.

Waivata International Limited (the purported chargee) had begun discussions with Smarter Way regarding the acquisition of Smarter Way’s business and assets. Smarter Way and Mr Jarvie requested Waivata to provide a short-term loan facility to Smarter Way of approximately $130,000. The Loan Facility Agreement provided that unless the parties entered into a binding Sale of Business Agreement by a specified date, Smarter Way must repay the principal, interest and costs.

No sale of business agreement was entered into and the money was not repaid by Smarter Way. Accordingly, Waivata tried to rely upon Clause 4 of the Loan Facility Agreement which provided that if Smarter Way did not repay the sum advanced in accordance with the Agreement:

"Waivata will immediately become the full and absolute beneficial owner of the business and the assets and, to the extent possible without further act or documentation, the legal owner of the business and the assets".

The Loan Facility Agreement provided that upon full and absolute ownership in the business and the assets passing to Waivata, Smarter Way would be discharged from any obligation to repay the debt.

Mandie J had to decide whether the Loan Facility Agreement (and in particular Clause 4) constituted a charge.

His Honour noted that broadly speaking a charge is a security interest and is the granting of an interest of some kind in property entitling the chargee to have resort to that property for the purpose of obtaining repayment. His Honour noted the distinction between a charge as a security interest in property on the one hand and a transfer of absolute ownership in property on the other.

Mandie J suggested that an agreement that property be transferred absolutely and beneficially to a lender upon non-payment of a debt by a specified date without any rights in the nature of an equity of redemption did not constitute a charge.

His Honour suggested that in the ordinary course repayment of a sum due should extinguish a charge if it is properly constituted.

Having concluded that the relevant Loan Facility Agreement did not constitute a charge, His Honour went on to consider whether Clause 4 could be given effect to in accordance with its terms.

Mandie J said there was much strength in the submission that Clause 4 imposed an unenforceable penalty for breach, having a value manifestly in excess of the likely loss (the amount of the unpaid debt plus interest and costs). His Honour was assisted by the evidence which established that Waivata had offered the sum of $2 million to purchase the business and assets; well in excess of the debt owed to Waivata. Having regard to His Honour’s view on the charge issue, he did not have to reach a conclusion on the enforceability issue.

This case is a timely reminder that the terms of any charging clause need to be carefully drafted to ensure a charge is properly constituted. The right to have the charge extinguished upon repayment of the principal debt and an associated "equity of redemption" may be important factors in finding a valid charge exists.

(C) ASIC POWERS DO NOT IMPINGE UPON THE COURT’S POWERS TO CONTROL INSPECTION OF DOCUMENTS DURING PROCEEDINGS

(By James Paterson, [Phillips Fox](http://www.phillipsfox.com.au))

Maronis Holdings Ltd v Nippon Credit Australia Ltd [2000] NSWSC 138, Supreme Court of New South Wales, Bryson J, 9 March 2000.

The full text of this judgment is available at:

"<http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2000/march/2000nswsc138.html>"

or "<http://cclsr.law.unimelb.edu.au/judgments/>".

(1) The dispute

The initial dispute between the parties related to commercial transactions and financing arrangements within the Girvan Group of companies some months or up to a year before financial difficulties overwhelmed it. In investigating the group’s financial activities, the Australian Securities Commission (‘ASC’) conducted a private examination in which a transcript record was produced.

All parties to the dispute were notified that documents from ASIC had been produced on subpoena, however the parties were not informed of the particular documents that had been provided.

The fourth defendant, Mr Ambler, obtained a direction allowing him immediate and preliminary access to the documents. Upon inspection of the documents produced by ASIC, Mr Ambler’s solicitors notified all parties to the dispute and ASIC that they had identified a document over which they were claiming privilege, and objected to access being granted to the parties.

The document in question was a transcript of an examination conducted by the then ASC pursuant to its compulsory powers under section 9 of the Australian Securities Commission Act 1989 (‘the Act’). The transcript was relevant to the question of whether Girvan Australia was trading whilst insolvent. The ASIC investigation arose out of the liquidation of Girvan Corporation and the financial difficulties of companies in the Girvan group, whilst the dispute in question here related to commercial transactions and financing arrangements within the Group some months or up to a year before the financial difficulties overwhelmed it. The defendant argued that:

(a) the documents contained confidential communications between the defendant and ASIC, which were obtained pursuant to the ASC’s compulsory powers;

(b) ASIC had acted in breach of its powers pursuant to section 127 of the Act;

(c) the defendant had been denied the protection afforded by section 25 of the Act; and

(d) the transcript did not contain information related to any of the issues raised in the proceeding, and therefore was irrelevant to the dispute.

Section 22 of the Act outlines the private nature of the examinations ASIC may conduct. Section 25 of the Act outlines the circumstances in which another person may obtain a copy of the transcript of the examination, which provides a protection of confidentiality to the person being examined. This confidentiality, however, must be balanced with the use of the information for its prescribed purposes. For example, disclosure to others may take place in the course of conducting a prosecution, or adducing evidence in a prosecution. ASIC is considered to have made an authorised disclosure if the record is obtained under section 25 of the Act.

Further, section 127(1) of the Act provides that ASIC shall take all reasonable measures to protect from unauthorised use or disclosure information given to it in confidence or in connection with the performance of its functions or the exercise of its powers.

The decision of the High Court of Australia in Johns v Australian Securities Commission (1993) 178 CLR 408 established that where ASIC produces a document to a court in compliance with a subpoena or other order of the court, the protection of confidentiality with respect to the documents comes under the control of that court, and is not under the control of ASIC. Therefore the Court must balance the confidential nature of the examination with the public interest considerations, such as the administration of justice, and the interests of litigants in having relevant evidence available for tender.

(2) Justice Bryson’s findings

(a) The objection relating to the confidentiality of the transcript was not a reason why the inspection of the documents should not occur (Justice Bryson did, however, state that the information would be restricted to the purpose of the conduct of these proceedings).

(b) The restrictions contained in section 25 and section 127 of the Act appear to extend to information given to ASIC in a private examination and also to the transcript record of that information. However, the production of a document in accordance with a subpoena is not disclosure under section 25 or section 127 of the Act. As ASIC has no choice about compliance, the exercise of producing a document does not fall within the concept of ‘disclosure’.

(c) The test to determine whether the document is relevant is not the same test as applied on objection to evidence. Rather, the Court may allow documents to be inspected if they are apparently relevant or are on the subject matter of the litigation, so it is not necessary that the document itself goes toward proving or disproving a fact in question.

(d) ASIC had not acted in breach of any obligation. The defendants had notice of the plaintiff’s application for access in these proceedings, and had a fair opportunity to debate it in Court.

(e) The fact that a procedure exists under section 25 of the Act for the release and use of the documents does not qualify and has no implications for the existence and availability of the Court’s powers to allow and control access and inspection. The powers of the Court are not taken away or diminished by implication from provisions of the Act. Justice Bryson considered that the reference to ‘unauthorised’ disclosure in section 127 of the Act recognised that disclosure may be required under the compulsion of law.

(D) DISCLOSURE REQUIREMENTS FOR EXPLANATORY MEMORANDUM IN MEMBERS’ SCHEME OF ARRANGEMENTS

(By Mark Stevens, [Phillips Fox](http://www.phillipsfox.com.au))

In Re Hudson Conway Limited [2000] VSC 21, Supreme Court of Victoria, Beach J, 21 January 2000.

The full text of this judgment is available at:

"<http://cclsr.law.unimelb.edu.au/judgments/states/vic/2000/january/2000vsc21.html>"

or "<http://cclsr.law.unimelb.edu.au/judgments/>".

This decision considered the application of two schemes of arrangement, both submitted by Hudson Conway Ltd (‘HCL’). The first scheme of arrangement was in relation to HCL’s members (‘the members’ scheme’), and the second was in relation to option holders of HCL (the optionholders’ scheme). Both schemes were subject to sections 411(4) and (6) of Corporations Law (‘the Law’).

The optionholders’ scheme proposed that all option holders receive one Publishing and Broadcasting Ltd (PBL) share for every 150 options held. This was unopposed by the members. The members’ scheme proposed that all shareholders (other than those associated with Mr Lloyd Williams) were to receive two shares in PBL for every three HCL shares held. This scheme was opposed by three shareholders: Peter Forbes MacLaren, and two companies of which he was a director. Their cumulative interests represented less than 0.03% of the company’s share capital.

Pursuant to sections 412(1), 412(6) and 412(8) of the Law, the Australian Securities and Investments Commission (‘ASIC’) has the authority to comment on the standard of disclosure in the Explanatory Memorandum (‘EM’) issued to the participants under the schemes of arrangement.

ASIC commissioned a report by Pricewaterhouse Coopers (‘PWC’) to review the sufficiency of disclosure to members under the EM, with particular focus on the independent expert’s report (‘the Hambros report’). HCL then sent to members copies of the PWC report along with additional reports from other independent experts commenting on the EM.

ASIC accepted the level of disclosure provided to members as sufficient for them to make an informed decision upon whether the scheme was in their best interests.

The members overwhelming voted in favour of the scheme and their approval was not opposed by ASIC. The EM and independent reports were also approved by the ASIC and Justice Gillard in earlier proceedings.

Mr Maclaren and the two companies of which he was a director objected to the scheme, claiming:

(a) the period of time allowed to members to make an informed decision based on the EM and the reports was insufficient;

(b) the EM unduly focused on the favourable reports relating to the members’ scheme, giving little prominence to the PWC report commissioned by ASIC. Further, no reasons were given for variously ignoring the contents of the PWC report, or for the preference given to the Hambros report, in breach of clause 8301 of Schedule 8 of the Corporations Regulations Schedule (‘the regulations’);

(c) the directors of HCL had either not stated, or not sufficiently stated, their reasons for recommending the proposal, as required under clause 8301 of the regulations;

(d) the directors did not give reasons why they had changed their strategy, as required under clause 8302(i) of the regulations;

(e) the Hambros report did not give reasons for not expressly considering the interests of Mr Williams. The Hambros report did not state the factors considered or the weight given to those factors or reasons for making its recommendation, as it is required to do pursuant to clause 8303 of the regulations.

Justice Beach dismissed all of the claims, and approved both schemes of arrangement.

His Honour found the four week period set by Justice Gillard to be ample time for the shareholders to consider the information, bearing in mind no other shareholder had complained that this period was too short. Further, Mr Maclaren had opportunity to raise the issue at the meeting to approve the scheme on 17 December 1999, and did not do so.

While the EM did not focus on the PWC report, it was referred to a number of times in the EM. Justice Beach considered this sufficient attention. A copy of the report was also sent to each of the shareholders. His Honour took into account the fact that the ASIC had approved the EM after careful examination and that Justice Gillard had also made an order approving the EM.

Justice Beach considered that the members of HCL were better judges of what was in their commercial interests than the court, following Re Chevron (Sydney) Ltd (1963) VR 249 at 255. It was the decision of the individual shareholder to determine the relevant weight to be given to each independent expert’s report and it was not incumbent upon shareholders to accept the views expressed by the directors or any one report. His Honour stated that ‘the fact that one independent expert report expressed a view in relation to the scheme contrary to the views of Hambros and the directors of HCL is no ground in the circumstances of this case for not approving the scheme’.

All aspects of the proposed scheme had been explained to shareholders together with the directors’ own reasons for arriving at their conclusions. Justice Beach stated that ‘it would be difficult to know what further material the directors could have provided concerning their reasons’. In his Honour’s opinion the directors had adequately explained their reasons. The question as to ‘whether these reasons were sound is not a matter for the court to decide’. The directors may determine the weight they wish to attach to each report. However, it is not the position of directors to point out to members why they preferred one report to another. This would be seen to be attempting to exert an influence on the decision of members.

His Honour believed it was not necessary for the independent expert’s report to consider the interests of Mr Williams. Clause 8303 of the regulations requires the expert to address the ‘best interest of the members of the company subject to the scheme’. The Hambros report had considered the interests stood to be gained by Mr Williams, and had conveyed to members the expert’s view as to what benefit might flow to Mr Williams.

In conclusion, Justice Beach found that members could not have been provided with more information about the proposal than they were given. ‘The court must leave it to the commercial sense of the creditors to judge what is reasonable in their interests’ (from Re Pheon Pty Ltd (1986) 47 SASR 427 at 435). According to his Honour, a similar observation could be made in relation to members who are considering a scheme of arrangement.

(E) THE NRMA JUDGMENT – DEMUTUALISATION UNDER SECTION 411 OF THE CORPORATIONS LAW

(By Danielle Dubois, Solicitor, [Clayton Utz](http://www.law.unimelb.edu.au/bulletins/archive/http//www.claytonutz.com.au), Brisbane)

NRMA Limited (Application of) [2000] NSWSC 82, Supreme Court of New South Wales, Santow J, 24 February 2000

The full text of this judgment is available at:

"<http://cclsr.law.unimelb.edu.au/judgments/states/nsw/2000/february/2000nswsc82.html>"

or "<http://cclsr.law.unimelb.edu.au/judgments>".

(1) Background

On 14 February 2000, Santow J ordered the convening of scheme meetings under section 411(1) of the Corporations Law to take place on 19 April 2000, so that the members of the NRMA Group could vote on the proposed demutualisation. Santow J’s extended judgment of 24 February 2000 sets out his reasons.

The boards of NRMA Limited ("Association") and NRMA Insurance ("Insurance"), which are both mutuals, proposed that their members have the opportunity to vote on the restructuring of the NRMA Group, whereby Insurance would be demutualised under Part 2B.7 of the Corporations Law, and convert to a public company limited by shares. All members of Association and Insurance would become shareholders in a new company, NRMA Insurance Group Ltd ("NIGL") which would be the sole shareholder of Insurance. Association would remain a mutual and various business relationships would be established between the three entities, to preserve their close relationship in key areas of common use.

The implementation of the proposal involved five schemes of arrangements; changes to the constitutions of Association and Insurance; approval of certain business relationship agreements by members of Insurance; and conversion of Insurance to a public company limited by shares.

Once the members approved the schemes of arrangement, Court approval and the approval of ASIC for Insurance’s application under Part 2B.7 would be needed. However all of this was conditional on the members subsequently voting for demutualisation.

(2) The role of the court in ordering a scheme meeting

Santow J pointed out the distinction that should be drawn between the role of the Court prior to approving the scheme meeting ("convening stage") and the role of the Court in considering whether to approve the scheme of arrangement after the members have voted in favour of the scheme ("approval stage").

At the approval stage, the Court pursuant to section 411(6) has the discretion to make orders approving the scheme. Following Court approval, the arrangement generally takes immediate effect in accordance with its terms. In the present case, each arrangement, after Court approval, would still be subject to termination if certain conditions subsequent were not fulfilled relating to the demutualisation steps.

Before ordering a meeting pursuant to section 411(1) of the Corporations Law, the Court must be satisfied with respect to a number of requirements including:-

(i) Disclosure - There must be proper disclosure in the explanatory statement as required by section 411(3). Essentially what is required is a statement of all the main facts as will enable shareholders to exercise their judgment on the proposed scheme. It is not for the Court to substitute its commercial judgment for that of properly informed shareholders or creditors, hence the emphasis on full disclosure.

(ii) "Arrangement" - The Court must be satisfied that the scheme can be properly described as an "arrangement" or "compromise" so as to come within the ambit of section 411. The word "arrangement" has been given a wide meaning and generally speaking, unless the arrangement is ultra vires the company or seeking to deal with a matter for which a special purpose is laid down by the Corporations Law, or to evade a restriction imposed by the Corporations Law, almost any arrangement otherwise legal which touches or concerns the rights and obligations of the company or its members or creditors, and which has been properly proposed, may come under section 411. Santow J did not consider the proposed schemes to be ultra vires and found that they were "arrangements".

(iii) Part 5.1 body - The Court must be satisfied that the company proposing the scheme is a Part 5.1 body. This was clearly satisfied as both companies were public companies limited by guarantee.

(iv) Schemes "properly proposed" - Section 411 of the Corporations Law gives jurisdiction to order scheme meetings only where the schemes are properly proposed. Santow J held that the proposals were not conceived for an improper purpose.

(v) ASIC - Section 411(2) provides that the Court shall not make an order to convene a meeting unless it is satisfied that ASIC has had a reasonable opportunity to examine the terms of the proposed arrangement and to make submissions to the Court. ASIC was given a reasonable opportunity to examine the terms of the proposed arrangement and make submissions to the Court. It was satisfied at a prima facie level with the disclosure contained in the information memorandum.

(3) The process thereafter leading to scheme approval or rejection

Santow J pointed out that, at the convening stage, the Court’s role is to ensure there has been compliance with the threshold statutory and regulatory requirements. The Court is not to determine the commercial efficacy of the proposed arrangement, or whether the arrangement is "just’ or "fair". Those issues are to be considered by the Court after the scheme has been approved by the members of the scheme company.

In some cases, Courts have taken the approach of looking at the merits of a scheme at the convening stage to determine whether it is likely the Court would approve the arrangement when it comes back for the approval stage under section 411(6). This has led to the practice of Courts at the convening stage, on the basis of the material placed before the Court, deciding whether it would be likely to approve the scheme, subject to any further argument or new matters being brought forward at the final approval process. Essentially, the Court is to be satisfied that there has been an absence of oppression and the compromise or arrangement is one which is capable of being accepted.

(4) The role of objectors

It was proposed that the Court make orders that Association and Insurance contribute money towards the legal costs of the objectors or provide an indemnity to the objectors amounting to a guarantee to pay the objectors’ costs on an indemnity basis and not seek an order for costs against the objectors.

Santow J reserved his decision on costs as this was only the convening stage but commented that usually scheme companies pay the objector’s costs, provided that the objections are not frivolous or without substance. However, if objectors are trying to stall a scheme of arrangement for their own purposes, then Courts will not hesitate to make a costs order against those objectors and even an indemnity cost order where appropriate.

(5) The use of conditions subsequent in the proposal

The proposal was unconventional in the sense that it contained conditions subsequent to Court approval, in particular demutulisation. If any of these conditions subsequent were not fulfilled by 31 December 2000, the schemes would be able to be terminated and the status quo effectively restored. Santow J did not object to this arrangement as it preserved certain capital gains tax advantages for members.

(6) Proxy and agency issues

A special feature of some of the schemes was the creation of an agency under which each company became invested with certain specific authorities to act on behalf of each relevant member in connection with particular implementation steps. This streamlining avoided the need for the vast bulk of members to meet after 19 April 2000 for the purposes of considering the various other resolutions required to complete the process. Unless a member expressly objected to the company becoming its agent, it would happen automatically and the company would be able to vote on behalf of the member at the meeting.

Santow J firstly looked at whether such an agency/proxy arrangement was legally valid and concluded that it was. He then looked at whether such a scheme proxy should be treated as so objectionable at this stage to be seen as a fatal impediment to approving the scheme.

One concern of Santow J was that this form of proxy took advantage of shareholder apathy, thereby shifting shareholding power in favour of management. In the circumstances, Santow J was satisfied there were exceptional circumstances to warrant the use of the scheme proxy for a later demutualisation resolution. However he reserved his final view for the scheme approval stage.

(7) Membership classes

The proposed classes of members were based on whether a member was a member of Insurance, Association or both. NRMA submitted that there was no need to divide those classes into further classes based on lesser differences between various types of membership or to categorise members by reference to numbers of years of membership or the number of insurance policies sold.

It was submitted that dividing the proposed classes into smaller classes would fracture the classes and may give a greater power to smaller groups to veto the arrangements.

Santow J was satisfied that the various sub-groups did not have such dissimilar interests as to make it impossible for them to consult together. However, he held the voting result at the relevant meetings would need to be closely scrutinised having regard to the potentially divergent interests, and therefore detailed records of the voting results should be kept, differentiating the members by the number of shares obtained under the share allocation formula.

(8) Equitable constraints

An issue was raised that the restructuring with its intended demutualisation and subsequent listing was constrained or precluded by the general intention and common understanding of the Insurance members at the time they became members (the Tivoli Freeholds principle).

Santow J rejected this proposal. In the absence of an express provision in the constitution that Insurance cannot change its company type, there is no reason why it cannot do so. He held that Tivoli Freeholds did not apply in the current circumstances and there was no constraint based on some common understanding of members incapable of alteration as would prevent a properly approved scheme of arrangement embracing the steps to demutualise.

(9) Is there a trust of Insurance’s assets?

The issue was raised whether Insurance was constitutionally able to demutualise. Its constitution provided that on the winding up or dissolution of the company, its residual assets should be transferred to NRMA or such other company with similar objects. This, it was argued, created a trust of the residual assets of Insurance following its winding up.

As part of the proposal, this provision would be altered to ensure Insurance remained a mutual insurance company within the meaning of the Income Tax Assessment Act so as to qualify for tax relief available in demutualisation pursuant to Division 9AA of Part III of the Act.

Santow J held that there was no basis for treating the constitution of Insurance as creating a trust of the residual asset of Insurance in favour of Association following its winding up. Nor was there any basis for preventing a subsequent change to that disposition of Insurance's residual assets on winding up as was proposed.

(10) Cut-off of membership

The Board of Association and Insurance resolved to publish a membership cut-off at midnight 25 February 1999 to protect the interests of current members. Association’s rules provided that the Board could refuse to admit any person as a member without providing a reason and secondly that the Board could close the register for up to 45 days before a meeting of members for the course of the voting period. It was argued that this latter rule, which had been added to the constitution in October 1998, was added for the purpose of demutulisation, although this was not disclosed to the members and therefore it was misleading and deceptive. Santow J rejected this proposal and held that there was no legal impediment to closing off membership of Association and Insurance for the purpose of limiting the schemes’ benefits to members prior to the cut-off date.

(11) Release of draft explanatory statement to the media

There was discussion as to whether the draft information memorandum should be released to the media. NRMA was against the proposal, arguing that if it was released in draft form, media reporting could infect public debate with confusion or misconception as the document would later be amended.

Santow J held that a draft information memorandum, being subject to material change, should not be released to the press until the meeting convening orders are made.

(12) Accounting and related issues

There was a complaint about Insurance’s accounts which included within the reported profit and loss since 1994, unrealised gains and losses on Insurance’s investment portfolio. It was argued that the proposal to list was a fraudulent scheme, as there was no way NRMA could legally pay dividends. This was because the dividends would not be paid out of profits, contrary to the requirements of section 254T of the Corporations Law. The submission relied on a previous judgment of Santow J in NRMA Ltd v Yates [1999] NSWSC 859. However, Santow J held that that case had dealt with the illegitimacy of aggregating an unrealised profit from an earlier year of income to the realised profit of a later year. Therefore Santow J rejected the submission and held that Insurance must include unrealised gains in its accounts and that dividends may be paid out of a combination of realised and unrealised gains without contravening section 254T of the Corporations Law, provided such combination produced a profit overall.

(13) Availability of section 411 procedure

It was submitted that NRMA was not entitled to approach the Court under section 411 of the Corporations Law, because that provision only applied to companies experiencing some kind of difficulty. Alternatively, it was submitted that the boards of Insurance and Association lacked clean hands and therefore were precluded from applying.

Santow J rejected this proposal of applying the equitable requirement of clean hands where no equitable remedy was sought and found in any event, that lack of clean hands was not demonstrated. He held that recourse to a scheme of arrangement under section 411 was not a privilege, but simply a statutory facility to bind members, once its requirements were satisfied. Those requirements were capable of being satisfied by the NRMA proposal if duly passed and approved and they would constitute an arrangement between members and the relevant scheme company.

(14) Mutual issues

It was argued that Insurance, as a mutual, could not lawfully demutualise due to past accumulation of surpluses and profits beyond those needed to provide prudentially for liability. Such accumulation was said to be the result of a failure in the directors’ alleged obligations.

In considering this issue, his Honour addressed the following issues:

(i) the nature and characteristic of a mutual;

(ii) directors’ duties with respect to price policies;

(iii) insurance members’ rights to dividends and surplus assets in winding up; and

(iv) the Australian position and other jurisdictions’ positions on whether a mutual can demutualise.

He concluded that "mutuality principles", the constitution of Insurance and the fact that there were accumulated profits derived from failure to pay rebate or carry out "mutuality pricing" did not constitute any legal impediment to the approval of the schemes with the associated demutualisation. This had been effected in other jurisdictions and cases. It was primarily a matter for members, properly informed, to decide for themselves.

(15) "Paying up" of shares in insurance and NIGL

The issue of whether the NIGL shares would be fully paid when issued to members of Insurance in return for them giving up membership rights, was raised. Santow J held that the NIGL shares would be "fully paid" upon issue with NIGL left as the sole shareholder of Insurance. Due to the abolition of par value there was no illegality in that.

(16) Conclusion

Santow J held that on all of the material placed before the Court at the convening stage, there were no legal impediments to approval of the scheme. However, the Court’s discretion to give or withhold approval remained unfettered for the approval stage under section 411(6) of the Corporations Law.

5. RECENT CORPORATE LAW JOURNAL ARTICLES

A Ding, ‘An Interpretation of the Equality of Opportunity Principle in the Context of Benefits Prohibited under the Corporations Law’ (2000) 18 Company and Securities Law Journal 6

A key foundation on which takeover regulation in Australia is based is the equality of opportunity principle. This article examines the development of the law with regard to the equality of opportunity principle commencing with the "uniform" Companies Act of 1961, such that an articulation of the meaning of equality of opportunity in the takeovers context can be made. In so doing, an understanding of the present day mechanisms by which equality of opportunity is intended to be conferred through sections 697 and 698 (sections 622 and 623 after the commencement of the Corporate Law Economic Reform Program Act 1999) should result. It also examines recent case law concerning those provisions with a view to determining whether the decisions in those cases reconcile with the underlying policy of the provisions. It then addresses the question of whether either section 697 or section 698 need reform having regard to the principle and whether reform is called for having regard to recent decisions which have considered the operation of those provisions. In conjunction with this, a summary of the Government-sponsored reviews of these two provisions is provided with a view to analysing the appropriateness or otherwise of the recommendations made as a result of their review.

N Calleja, ‘Current Issues Relating to Prospectus Advertising and Securities Hawking’ (2000) 18 Company and Securities Law Journal 23

As national boundaries become increasingly permeable due to technological advances like the Internet and various other forms of electronic commerce, regulators are finding that the laws with which they arm themselves are inadequate. In a climate in which investment scams are on the rise, the laws in relation to prospectus advertising and securities hawking come sharply into focus. This article examines current Australian laws and the new Corporate Law Economic Reform Program Act 1999 (Cth) pertaining to prospectus advertising and securities hawking and analyses whether the law is able to deal with recent developments. The article also examines the equivalent laws in the United States of America and Hong Kong. This article concludes that while the new provisions in the CLERP Act amendments in relating are laudable, they, in some instances, fall short of their objectives. For example, the provisions probably do not deal adequately with certain issues such as the Internet and electronic commerce.

K Bennetts, ‘Dealing with Winding Up Applications Following the Appointment of an Administrator’ (2000) 18 Company and Securities Law Journal 41

In this article, the author describes the legal position of the unsecured creditor of a company who, prior to the company’s appointment of an administrator, has filed an application with the court for the winding up of the company. The article is particularly concerned with the manner in which the courts, in hearings under section 440A(2), Corporations Law, have dealt with winding up applications in these circumstances, and the reasons offered by the courts in allowing one process to prevail over the other.

Note: ‘Recent Developments Relating to Pre-Receivership Contracts’ (2000) 18 Company and Securities Law Journal 50

Note: ‘GIO, Earthquakes and Hurricanes: An Overview of Catastrophe-Linked Securities and Other Innovations’ (2000) 18 Company and Securities Law Journal 62

Note, ‘Competition and the Independence of the Auditor-General’ (2000) 18 Company and Securities Law Journal 67

M Bos, ‘Transactions Having Preferential Effect – The Running Account Principle Applied in New Zealand’ (1999) 7 Insolvency Law Journal 174

In Australia the running account principle is well established as a defence to an action by a liquidator for recovery of alleged voidable preferences. However, in two New Zealand High Court decisions (Chatfield v Mercury Energy Ltd and Re Island Bay Masonry Ltd; Firth Industries v Gray) the running account principle was rejected as a defence under New Zealand’s current voidable preference regime. This article examines how the running account principle has been established in Australia and considers whether the principle can apply in New Zealand. In conclusion, it is submitted that the running account principle should apply under New Zealand’s current voidable preference regime.

D Morrison and C Anderson, ‘Uncommercial Transactions – Developments in the New Regime’ (1999) 7 Insolvency Law Journal 184

This article examines the nature of the reform brought about by the Corporate Law Reform Act 1992 (Cth), and how subsequent court decisions have interpreted and applied the new provisions. First, the article considers the history and development of the legislation within the context of the section 588FB requirement for insolvency. Secondly, it considers the ambit of the cases regarding: the interpretation of the statute; the difficulty of determining value in the context of "commerciality"; and the ambit of the kinds of transactions that might be caught by the application of the legislation. Finally the article makes conclusions for the efficacious operation of the provisions.

K Eagle, ‘Evidentiary Issues in Insolvency’ (1999) 7 Insolvency Law Journal 196

This article examines some of the evidentiary issues that arise when a liquidator attempts to prove the insolvency of a company in liquidation. The case law and statutes that have, over the years, dealt with those issues are considered in a practical light.

L Taylor, ‘The Derivative Action in the Companies Act 1993’ (1999) 7 Canterbury Law Review 314

W Laufer, ‘Corporate Liability, Risk Shifting, and the Paradox of Compliance’ (1999) 52 Vanderbilt Law Review 1343

A Greenhow, ‘The Statutory Business Judgment Rule: Putting the Wind into Directors’ Sails’ (1999) 11 Bond Law Review 33

C Free, ‘Limiting Auditors’ Liability’ (1999) 11 Bond Law Review 118

P Regan, ‘Great Expectations? A Contract Law Analysis for Preclusive Corporate Lockups’ (1999) 21 Cardozo Law Review 1

P Dalley, ‘The Law of Partner Expulsions: Fiduciary Duty and Good Faith’ (1999) 21 Cardozo Law Review 181

V Yeo, ‘Corporate Governance in the Information Age: The Impact of Information Technology and Emerging Legal Issues’ (1999) 20 Hong Kong Law Journal 194

A Nijenhuis, ‘Main Aspects of EU Regulation on Derivatives’ (1999) 10 European Business Law Review 193

J Karns and J Hunt, ‘Corporate Executive Deferred Compensation: Should the Exercise of Stock Appreciation Rights Trigger Securities Law Liability?’ (1999) 75 North Dakota Law Review 535

S Fridman, ‘Conflict of Interest, Accountability and Corporate Governance: The Case of the IOC and SOCOG’ (1999) 22 (No 2) University of New South Wales Law Journal

M Fox, ‘Retaining Mandatory Securities Disclosure: Why Issuer Choice is not Investor Empowerment’ (1999) 85 (No 7) Virginia Law Review

C Yablon, ‘Bonus Questions – Executive Compensation in the Era of Pay for Performance’ (1999) 75 Notre Dame Law Review 271

N Kim, ‘Malone v Brincat: The Fiduciary Disclosure Duty of Corporate Directors Under Delaware Law’ (1999) 74 (No 4) Washington Law Review

R Campbell, ‘Fair Value and Fair Price in Corporate Acquisitions (1999) 78 (No 1) North Carolina Law Review

R Traband, ‘The Case Against Applying the Co-Conspiracy Venue Theory in Private Securities Actions’ (1999) 52 (No 1) Rutgers Law Review

M Berkahn, ‘A Statutory Business Judgment Rule’ (1999) 3 Southern Cross University Law Review 215

S Watson, ‘Liability of Auditors to Third Parties in New Zealand: Clarification At Last’ [2000] Journal of Business Law 1

S Prakash, ‘Our Disfunctional Insider Trading Regime’ (1999) 99 (No 6) Columbia Law Review

R Langton and L Trotman, ‘Defining "The Best Interests of the Corporation": Some Australian Reform Proposals’ (1999) 3 Flinders Journal of Law Reform 163

‘The Rights of Shareholders in Shareholding Companies Under Vietnam’s Law on Enterprises’ (1999) 6 (No 64) Vietnam Law and Legal Forum

D Langevoort, ‘Half Truths: Protecting Mistaken Inferences by Investors and Others’ (1999) 52 (No 1) Stanford Law Review

L Bebchuk and M Roe, ‘A Theory of Past Dependence in Corporate Ownership and Governance’ (1999) 52 (No 1) Stanford Law Review

S Schwarcz, ‘The Inherent Irrationality of Judgment Proofing’ (1999) 52 (No 1) Stanford Law Review

L LoPucki, ‘Contract Bankruptcy: A Reply to Alan Schwartz’ (1999) 109 Yale Law Journal 317

M Klock, ‘The SEC’s New Regulation ATS: Placing the Myth of Market Fragmention Ahead of Economic Theory and Evidence’ (1999) 51 Florida Law Review 753

C Bradford, ‘Expanding the Investment Company Act: The SEC’s Manipulation of the Definition of Security’ (1999) 60 (No 3) Ohio State Law Journal

T Smith, ‘The Efficient Norm for Corporate Law: A Neo-Traditional Interpretation of Fiduciary Duty’ (1999) 98 Michigan Law Review 214

G McGinty, ‘Directors’ Duties of Skill and Care in the UK and the Year 2000 Computer Problem’ (1999) 7 (No 3) International Journal of Law and Information Technology

Administrative Law Review, Vol 51 No 4, Fall 1999. Special Issue on the Securities and Exchange Commission. Articles are:

- Chairman A Levitt, ‘Plain Talk About On-Line Investing’

- Commissioner I Hunt, ‘It’s a Small World After all: The SEC’s Role in Securities Regulation Globalization’

- Commissioner L Unger, ‘Corporate Communications Without Violations’

- R Ferrara and P Khinda, ‘SEC Enforcement Proceedings: Strategic Considerations for When the Agency Comes Calling’

- A Smith, ‘SEC Cease and Desist Orders’

- J Walsh, ‘Regulatory Supervision by the Securities and Exchange Commission: Examinations in a Disclosure-Enforcement Agency’

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6. NEW CLERP BOOKS

(A) H A J Ford, R P Austin and I M Ramsay, "An Introduction to the CLERP Act 1999 – Australia’s New Company Law", Butterworths, 2000, ISBN 0 409 31761 6, 124 pages, $25.

Butterworths Customer Service is fax: (02) 9422 2405; tel: 1800 648 825

(B) R Baxt, I Ramsay, I Renard, R Simkiss and J Webster, "CLERP Explained", CCH Australia Limited, 2000, ISBN 1864 68 291 4, 283 pages, $70.

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